TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1936

No. 354

CAROLINE R. KUEHNER AND FREDERICK G. FISCHER, AS TRUSTEES, PETITIONERS,

vs.

GRAYSON M-P. MURPHY, ET AL., ETC.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED SEPTEMBER 10, 1936.

CERTIORARI GRANTED OCTOBER 26, 1936.

SUPREME COURT OF THE UNITED STATES

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vs.

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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1

UNITED STATES CIRCUIT COURT OF APPEALS,

FOR THE SECOND CIRCUIT.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER,
as trustees,
Appellants,

2

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Appellees.

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Cross-Appellants,

CAROLINE R. KUEHNER and FREDERICK G. FISCHER,
as trustees, et al.,
Cross-Appellees.

(Cross Appeals.)

3

Statement Pursuant to Rule No. XIII.

This proceeding was commenced in the United States District Court for the Southern District of New York on or about October 5, 1934, by the filing of a proof of claim, sworn to October 5, 1934, by the claimants, Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, deceased. United Cigar Stores Company of America, the above-named Debtor, a

former tenant of the predecessors in interest of the claimants, filed its petition for reorganization under Section 77B of the Bankruptcy Act on or about June 9, 1934.

The original parties to the proceeding instituted by the above-mentioned claimants were said claimants, Irving Trust Company, as trustee of the estate of the Debtor, and certain intervenors,—to wit, Grayson M-P. Murphy, et al., as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, et al., as a Debentureholders' Protective Committee, United Stores Corporation, Jacob Ruppert Realty Corporation, and Peter Grimm, et al., as a Landlords' Protective Committee. United Stores Corporation subsequently withdrew as an intervenor and by its petition verified November 22, 1935, Phoenix Securities Corporation prayed leave to intervene, which leave was subsequently granted. The Debtor never appeared at the hearings before the Special Master on the trustee's objections to the claim set forth in the aforesaid proof of claim nor at the hearing in said District Court upon the exceptions filed by the claimants, the above-mentioned Preferred Stockholders' Protective Committee, and the above-mentioned Debentureholders' Protective Committee to the report of the Special Master; and counsel for the Debtor have notified counsel for the claimants that it is not necessary to secure their consent to nor serve upon them copies of this transcript of record.

Irving Trust Company, as trustee of the estate of the Debtor, served upon counsel for the claimants on or about May 22, 1935, a copy of its petition praying that a time be fixed by the Hon. Irwin Kurtz, Special Master to whom said District Court had by its order dated July 17, 1934, re-

ferred all claims for consideration and report, for hearing its objections to said claim and also a notice notifying the claimants that such hearing would be held on June 4, 1935. 7

The hearing before the Special Master on the trustee's objections was held before Hon. Irwin Kurtz, Special Master as aforesaid, on May 22, 1935, and was adjourned to June 24, 1935.

The report of the Special Master dated October 23, 1935, recommended that the claim be allowed in part and that the question of the validity and rank of the remaining portion of the claim should be reserved for future determination.

On or about February 5, 1936, an order was entered by the District Court confirming in part and overruling in part said report of the Special Master, and both the above-mentioned claimants and the above-mentioned Preferred Stockholders' Protective Committee and the above-mentioned Debentureholders' Protective Committee have taken appeals from said order. The orders of said District Court allowing said appeals were dated March 4, 1936. 8

No parties have been arrested or bail taken or property attached or arrested, and the Debtor's estate is in the possession of Irving Trust Company, as trustee as aforesaid. 9

Proof of Claim.

10 UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

11 ---

United States of America,
District of —ss.:

At the City of Trenton, County of Mercer, State of New Jersey, on the date hereinafter set forth, came CAROLINE R. KUEHNER and FREDERICK G. FISCHER and made oath and say that:

I.

We, Caroline R. Kuehner and Frederick G. Fischer, individually and as trustees of the Es-
12 tate of Adam Fischer, deceased, acting under our authority as trustees, and duly authorized to make this proof as such, and as representing the ultimate beneficiaries under the last will of Adam Fischer, deceased, who joined in the execution of the lease hereinafter referred to because of our interest in said premises as remaindermen or otherwise, and in behalf of the heirs and next of kin of Edward A. Fischer, deceased, and late trustee of the estate of Adam Fischer, deceased, the said Frederick G. Fischer having been duly appointed and qualified as co-trustee under said

last will of Adam Fischer, deceased, in the place 13
and stead of the said Edward A. Fischer, now deceased. We, the said trustees, being still in control of the property described in said lease and entitled to collect the rents and profits of the same, and in full charge of the management and control of said property.

II.

United Cigar Stores Company of America, the corporation which is the debtor in the above-entitled proceeding for reorganization (hereinafter called the Debtor), on August 29, 1932, 14
filed its voluntary petition in bankruptcy and was adjudicated a bankrupt in a proceeding in the above-mentioned Court (Docket No. 55129), and Irving Trust Company was appointed trustee in bankruptcy of said bankrupt and acted as such trustee in bankruptcy (herein called the Trustee in Bankruptcy) until June 14, 1934, the date of approval of the petition herein.

The claimant is the present owner of a claim against the Debtor, based upon or arising out of the lease dated October 18th, 1926 between Edward A. Fischer and Caroline R. Kuehner indi- 15
vidually and as executors and trustees of the Estate of Adam Fischer, dec'd, and Frederick G. Fischer, Margaret G. Fischer, Margarette Hensler, Louis Fischer, Jr. and Ruth Fischer, as Landlord, and the Debtor, as Tenant, covering the premises described therein, for a term commencing prior to August 29, 1932, and ending on March 31st, 1946, or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy on or about November 14th, 1932, or for damages or indemnity under a covenant or covenants contained in said lease.

16 The Trustee in Bankruptcy surrendered the premises covered by said lease on November 14th, 1932.

[Insert date on which possession of premises was turned over, or, if that date is not known, insert date of notice from Trustee in Bankruptcy that lease was rejected.] The landlord reentered said premises on November 15th, 1932.

Except to the extent hereinafter shown, neither the Debtor nor the Trustee in Bankruptcy has paid the rent or other obligations accruing under said lease after the 1st day of September, 1932.

[If the claimant is not the landlord named in the above-described lease, give explanation of how ownership of the claim was acquired, *i. e.*, by purchase of the premises, assign-
17 ment, inheritance, or otherwise:]

III.

The Debtor was on and before June 14, 1934, the date of the approval of the petition herein, and still is, justly and truly indebted to the claimant for amounts payable under said lease or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy or for damages or indemnity under a covenant or covenants contained in said lease, computed as follows:

18	Total net or fixed rent for entire term which has not been paid by the Debtor	$151,083.33	
	Total taxes, insurance, assessments, water rents or rates and other payments required to be made by Debtor for entire term which have not been paid by the Debtor (use actual amounts so far as known and estimates for the future—see footnote 1)	1,326.80	(last 4 mos. 1932) taxes
		2,917.09	(year 1933) "
		3,142.80	(" 1934) "
		33,750.00	(estimated at $3,000. per year for 11 years and 3 mos.)
	Total lease obligations which have not been paid by the Debtor		$192,220.02

Less:

Fair rental value of leased premises from date of rejection of lease to end of term (see footnote 2)	$100,250.00	
Dividends paid in bankruptcy proceedings on any claim based on original lease	1,110.34	
Amount paid by Trustee in Bankruptcy for use and occupation of premises by such trustee	646.77	
Amounts paid by subtenants of Debtor to landlord under original lease for occupancy up to date of rejection of lease	0.00	
		$102,007.11
Total amount claimed for entire term of original lease		$ 90,212.91

Claim is hereby made against the Debtor in the amount above set forth, together with such interest thereon as may be allowed by law.

1. Explain how future taxes, etc., are estimated: Taxes are estimated at $3,000. a year, based on average of last 3 years which are about $1,000. less per year than the previous 3 year period.

2. If all or any part of the leased premises was relet to another tenant for all or any part of the balance of the term of the original lease, the terms of the new lease should be taken into consideration in making this estimate; a copy of the new lease should be attached to this proof of claim, marked Exhibit A, and the following information should be supplied:

Name of new tenant: SaLee Shoppe, Inc., and Barney Oiitzsky.
Date of commencement of term of new lease: 4.1.1933 —10.21.1933.
Date of expiration of term of new lease:
Net or fixed rent per year under new lease: $
Taxes and other payments per year under new lease: $ (See copies of leases hereto annexed.)

Explain how future taxes, etc., are estimated:

State also any other facts on which estimate of fair rental value is based, stating such facts, if necessary, on a separate page as a schedule hereto:

22 Present tenants not holding leases are as follows: Charles C. Wacks, 3d floor front, $20.00 per month from July 15th, 1934, monthly tenant; Piat (first name unknown) one living apartment on fourth floor, $25.00 per month, from May 1st, 1934; E. A. Devlin, fourth floor rear, $22.50 per month from January 1st, 1933. All these are monthly tenants, holding from month to month.

Fair rental values are estimated to be a gross of $500.00 a month collectible rent, and this is allowed from date of surrender of premises November 14th, 1932, although as per leases, copies of which are attached, there was a period of several months of vacancies before tenants could be had. The present gross rent is $507.00 per month, from which only $7.00 a month is deducted for losses and vacancies. Experience since surrender of the lease indicates that approximately $500.00 per month is the largest rent return which can be expected from the property. The tenant for the LaSalle Shoppe, Inc., ground floor, has applied for a reduction of rent and it is by no means certain that this first floor can be continued to rent under as favorable terms as the present
23 lease, even during the time of its lease. Nothing has been received from lease above the fixed minimum rent. New leases require claimant to heat entire building and pay water rent and insurance, and taxes.

IV.

This claim in the amount above set forth, together with interest thereon as aforesaid, is allowable on a parity with debts which would be provable under Section 63 (a) of the Bankruptcy Act to the extent of the amount provided in subdivision (b) of Section 77B of the Bankruptcy Act, which said amount is computed as follows:

24 Net or fixed rent accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor	$2,187.50
Taxes, assessments, insurance, water rents or rates and other payments accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor	829.25

Total lease obligations accrued up to date of surrender of premises or date of reentry by landlord, whichever first occurred, and not paid by the Debtor		$3,016.75	25
Less:			
Dividends paid in the bankruptcy proceeding on any claim based on original lease	$1,110.34		
Amount paid by Trustee in Bankruptcy for use and occupation of premises by said trustee	646.77		
Amounts paid by subtenants of Debtor to landlord under original lease for occupancy up to date of surrender of premises or date of reentry by landlord, whichever first occurred	0.00		26
Unpaid lease obligations accrued up to date of surrender or reentry, whichever first occurred		$2,187.50	
Net or fixed rent reserved in lease (without acceleration) for three years next succeeding date of surrender of premises or date of reentry by landlord, whichever first occurred, or for entire balance of term if less than three years	$31,500.00		27
Taxes, assessments, insurance, water rents or rates and other payments to be made by Debtor during three years next succeeding date of surrender of premises or date of reentry by landlord, whichever first occurred, or for entire balance of term if less than three years	9,386.69		

28	Total lease obligations for three year period above described, or for entire balance of term if less than three years	40,886.69
	Total amount of claim allowable under Section 77B on a parity with debts which would be provable under Section 63 (a)	$43,074.19

Claim is hereby made against the Debtor in the amount above set forth, together with such interest thereon as may be allowed by law, on a parity with debts which would be provable under
29 said Section 63 (a).

V.

To the extent that the total amount of the claim for the entire term of the original lease, as hereinabove set forth in subdivision III hereof, is not allowable on a parity with debts which would be provable under said Section 63 (a), said claim should be allowed in subordination to debts so provable, but in priority to the claims or interests of holders of preferred and common stock of the Debtor.

30

VI.

No part of the claim herein asserted has been paid, and there are no setoffs or counterclaims thereto except as follows: $646.77 Moneys received for use and occupation from trustee in bankruptcy, between date of adjudication and date of surrender of lease. The claimant has not nor has any person for or on behalf of the claimant, to deponent's knowledge or belief, had or received, for the use or benefit of the claimant, any security

for said debt, except as follows: None. No judgment has been rendered therefor, nor for any part thereof, but a claim based on said lease was filed in said bankruptcy proceeding and was allowed in the amount of $893.89 and $663.40—Claim No. 2099—Lease No. 439. 31

In executing and filing this proof of claim, the claimant in no way waives any rights which the claimant may have to reclaim specific assets and expressly reserves such rights.

FREDERICK G. FISCHER L. S.
CAROLINE R. KUEHNER L. S.
Individually and as trustees under the last will of Adam Fischer, deceased, and as agents for the ultimate beneficiaries under said will. 32

Address to which all notices should be mailed:
Harvey T. Satterthwaite, Att'y,
137 E. State Street,
Trenton, N. J.

Subscribed and sworn to before me
this 5th day of October, 1934. 33

SARA A. SATTERTHWAITE,
Notary Public.

Notice of Hearing on Trustee's Objections to Claim.

34 DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation—No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

PLEASE TAKE NOTICE that upon the annexed petition of Irving Trust Company, Trustee of the estate of the above-named Debtor, verified May 17, 1935, a hearing will be held before Hon. Irwin Kurtz, Special Master, at 15 Park Row, Borough of Manhattan, City of New York, N. Y., on June 4th, 1935, at 3:00 o'clock in the afternoon, or as soon thereafter as counsel may be heard, and that at said hearing the undersigned will move this Court to have the claim referred to in said petition reduced to an amount found by the Court to be properly allowable in these proceedings.

35

Dated, New York, N. Y., May 21, 1935.

36

Yours, etc.,

CRAVATH, DE GERSDORFF,
SWAINE & WOOD,
Attorneys and Solicitors for
Irving Trust Company,
Trustee of the estate of
United Cigar Stores Company of America, Debtor,
Office and Post Office Address,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

Notice of Hearing on Trustee's Objections to Claim.

37

To:

HARVEY T. SATTERTHWAITE,
137 E. State Street,
Trenton, N. J.

ROSENBERG, GOLDMARK & COLIN,
165 Broadway,
New York, N. Y.,
Attorneys for Debtor.

M. CARL LEVINE,
535 Fifth Avenue,
New York, N. Y., 38
Attorney for Jacob Ruppert Realty Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
20 Exchange Place,
New York, N. Y.

and

RALPH MONTGOMERY ARKUSH,
15 Broad Street,
New York, N. Y.
Attorneys for Landlords' Protective Committee. 39

SHEARMAN & STERLING,
55 Wall Street,
New York, N. Y.

and

BERLE & BERLE,
70 Pine Street,
New York, N. Y.
Attorneys for Preferred Stockholders' Protective Committee.

Petition of Trustee for Hearing its Objections to Claim.

40

DAVIS, POLK, WARDWELL, GARDINER & REED,
15 Broad Street,
New York, N. Y.
Attorneys for Debentureholders Protective Committee.

SULLIVAN & CROMWELL,
48 Wall Street,
New York, N. Y.
Attorneys for United Stores Corporation.

41

Petition of Trustee for Hearing Its Objections to Claim.

DISTRICT COURT OF THE UNITED STATES.

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation—No. 59,886.

In the Matter

of

42

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

To the Honorable Irwin Kurtz, Special Master:

The petition of Irving Trust Company, as Trustee of the estate of the above-named Debtor, respectfully shows to the Court as follows:

On June 14, 1934, your petitioner was duly appointed temporarily and qualified as Trustee of

Petition of Trustee for Hearing its Objections to Claim.

the estate of the above-named Debtor, and on July 17, 1934, the appointment of your petitioner as Trustee was made permanent.

There has been filed with this Court a proof of claim numbered 5184 by Caroline R. Kuehner and Frederick G. Fischer, individually and as Trustees of the Estate of Adam Fischer, deceased, and as agents for the ultimate beneficiaries under said will (hereinafter called the Claimant) setting forth an alleged claim of the Claimant against the Debtor in the sum of $90,212.91 w/int. Your petitioner objects to the allowance in full of said claim for the following reasons:

The Trustee objects to the allowance of this claim as filed and asks that it be reduced to an amount limited as provided by statute. The trustee is advised that to the extent that the total amount of the injury alleged to have been sustained by the claimants resulting from the rejection of the lease upon which the claim is based by the Trustee in Bankruptcy exceeds an amount so limited, said claim is not, as set forth in the proof of claim, entitled to be allowed in these proceedings in subordination to debts which would be provable under Section 63 (a) of the Bankruptcy Act, but in priority to interests of holders of preferred and common stock of the Debtor.

Your petitioner, accordingly, desires to have its objections to said claim heard and considered, and said claim reduced to an amount found by this Court to be properly allowable in these proceedings.

This petition and all proceedings had thereon are not intended to affect in any way, or to waive any rights of your petitioner in regard to, the questions reserved by the Court for further deter-

46 mination as provided in its order of July 17, 1934 as amended, and, except as specifically stated in the foregoing objections, your petitioner reserves its right of objection, as provided by order of this Court dated November 13, 1934, with respect to all questions relating to the scrutiny of the circumstances of an assignment of future rent claims and the amount of the consideration paid for such assignment in determining the amount of damages to be allowed the assignee thereof, and the limitation of claims filed by committee members or agents to the actual consideration paid
47 therefor.

WHEREFORE, your petitioner respectfully requests that a time be fixed by this Court for hearing your petitioner's objections to said claim of which due notice to the Claimant and to all persons and parties who have intervened in these proceedings, or to their attorneys, shall be given by mail.

Dated, May 17, 1935.

48 IRVING TRUST COMPANY,
as Trustee of the estate of United Cigar Stores Company of America, Debtor,
By JOSEPH T. STEARNS,
Assistant Secretary.

CRAVATH, DE GERSDORFF, SWAINE & WOOD,
Attorneys and Solicitors for said Trustee,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

Petition of Trustee for Hearing its Objections to Claim.

49

United States of America,
Southern District of New York,
State of New York,
County of New York—ss.:

JOSEPH T. STEARNS, being duly sworn, deposes and says that he is an Assistant Secretary of Irving Trust Company, the petitioner herein, and that he has read the foregoing petition and knows the contents thereof, and is informed and verily believes that the same is true.

JOSEPH T. STEARNS. 50

Subscribed and sworn to before me
this 17th day of May, 1935.

ANNE L. RANDBY,
Notary Public,
Kings County.
Kings Co. Clk's No. 376, Reg. No. 7051.
N. Y. Co. Clk's No. 25, Reg. No. 7 R 64.
Cer. filed N. Y. Co.
Commission expires March 30, 1937.

51

Minutes of Hearing on Objection to Claim.

52

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

(In Bankruptcy.)

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

53

New York, June 24, 1935.

2:30 o'clock, P. M.

Before—IRWIN KURTZ, ESQ., *Special Master*.

HEARING ON OBJECTION TO CLAIM OF CAROLINE R. KUEHNER AND FREDERICK G. FISCHER AS TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF ADAM FISCHER, DECEASED, CLAIM DESIGNATED AS

54 No. 5184.

PROCEEDED PURSUANT TO ADJOURNMENT.

APPEARANCES:

MESSRS. CRAVATH, DEGERSDORFF, SWAINE & WOOD, Attorneys for the Trustee, by Donald C. Swatland and B. R. Shute, Esqrs., of Counsel.

MESSRS. MITCHELL, TAYLOR, CAPRON & MARSH, Attorneys for the Claimant, by Henry L. Glenn, Esq., of Counsel.

MESSRS. DAVIS, POLK, WARDWELL, GARDINER & REED, Attorneys for Debentureholders Committee, Intervenor, by Edgar G. Crossman, Esq., of Counsel. 55

MESSRS. SHEARMAN & STERLING, Attorneys for Preferred Stockholders' Protective Committee, Intervenor, by Douglas Steimle, Esq., of Counsel, and

MESSRS. BERLE & BERLE, Associate Counsel, by Winthrop H. Kellogg, Esq., of Counsel.

MESSRS. SULLIVAN & CROMWELL, Attorneys for United Stores Realty Corporation, Intervenor, by Alexander M. Grean, Jr. Esq., of Counsel. 56

M. CARL LEVINE, ESQ., Attorney for Jacob Ruppert Realty Corporation and other Creditors, Intervenors, by David Morgulas, Esq., of Counsel.

MESSRS. SMYTH & TUTTLE, Attorneys for Trustees of Cigar Stores Realty Holdings, Inc., Intervenor, by Bruce R. Tuttle, Esq., of Counsel.

The Master: This is claim No. 5184 of Caroline R. Kuehner and Frederick G. Fischer, individually and as trustees under the will of Adam Fischer, deceased. The claim is filed in the sum of $90,212.91. 57

(Discussion off the record.)

Mr. Shute: The trustee objected to the allowance of this claim as it was filed and asked that it be reduced to the amount limited by statute, to-wit, the three-year limitation.

The real estate department of the trustee had investigated the claim as filed and found that the fair rental value which was allowed in the claim was a reasonable one and one that we approve. The only remaining question then was

58 the one reducing it to the statutory maximum, and although that amount is not set forth in the motion papers it was—the statutory maximum was—$41,699.38.

The Master: Now off the record.

(Further discussion off the record.)

Mr. Kellogg: Is there any dispute about the three-year maximum here, Mr. Glenn, that the claim is allowable for the amount that has been suggested by Mr. Shute?

Mr. Glenn: There was not at the time we were trying to get the three-year rent claim allowed, but now that we have to prove the actual
59 amount of damages the way we compute it now is about $43,000 or $44,000.

Mr. Grean: May I ask does that three-year amount include taxes?

Mr. Glenn: Yes.

This claim, your Honor, as I understand it, is a test case which has been chosen to test out two legal questions principally, one the validity of the excess of the landlord's claim over the statutory parity claim, as I describe it—not the statutory maximum claim, and the other the question of the present provability of the dam-
60 ages sustained by this landlord.

The lease is a long term lease and the lease contains the usual covenant of indemnity whereby in the event of the termination of the lease by the landlord as the result of the default of the tenant the tenant covenants to indemnify the landlord against any loss of rent incurred throughout the remainder of the term.

The counsel for the preferred stockholders' committee and the debentureholders' committee take the position, as I understand, that such claim is not presently provable because under the doctrine

of Hermitage against Levine there is no sure way of determining the loss of rent to be suffered by this landlord until the expiration of the term. Counsel have shown an unusual amount of co-operation in signing two stipulations of fact which we believe contain all the material facts for the settlement of these two questions. 61

The Master: Mark them in evidence.

Mr. Glenn: I offer them in evidence.

Mr. Kellogg: Your Honor, we have objection as to the relevancy and materiality of parts of these stipulations.

May I have, Mr. Grean, my copy of the stipulation? (Document is handed to Mr. Kellogg by Mr. Grean.) 62

Mr. Kellogg: The stipulation provides—the main stipulation provides at the end thereof, that this stipulation is made without prejudice to the right of any of the undersigned to object to the admission of this stipulation in whole or in part on the ground that it or any part thereof is irrelevant or immaterial, but all other possible grounds of objection to its admissibility or to the admissibility of any of the facts are hereby waived.

I would like to state first the parts of the principal stipulation. 63

The Master: Mark it for identification.

Mark first the original stipulation, then the—(interrupted by)

Mr. Kellogg: Off the record, your Honor.

The Master: Mark the one that Mr. Kellogg is now objecting to, the main stipulation so-called.

(Document referred to is marked, "Trustee's Exhibit 1 for Identification", of this date.)

The Master: Off the record.

64 (Further discussion off the record.)

Mr. Kellogg: We object to the parts of this stipulation which is marked as Trustee's Exhibit 1 for Identification, which are as follows:

The Master: May I see it, Mr. Glenn? (Document is handed to the Master.)

Mr. Kellogg (continuing): Beginning at the top of page 3 of this stipulation and ending at the bottom of page 3; that is, our stipulation goes to all of the matter which is set forth on page 3 of the stipulation.

We also object—(interrupted by)

The Master: Objection overruled.

65 Mr. Kellogg: I have not stated, your Honor, the full grounds for my objection.

The Master: I thought you had.

Mr. Kellogg: There were other parts which I am going to refer to.

The Master: All right.

Mr. Kellogg: We also object to the part of this stipulation which begins in the middle of page 5 with the paragraph which starts, "The amount received", beginning at that point and following over to the middle of page 6, the paragraph ending, "during the period of his tenancy".

66 Mr. Crossman: The second paragraph.

Mr. Kellogg: Pardon me.

The Master: Which paragraph; including the third paragraph or the second?

Mr. Kellogg: Including the third paragraph, your Honor, in the middle of the page.

The provision of this lease with regard to defaults is found in article "Tenth" thereof and it is to the effect that if the tenant defaults in the lease, if the lease should be taken on execution or if the tenant should be adjudicated a bankrupt, or if any assignment of this property should be

made for the benefit of creditors then in any of 67
such cases the landlord may lawfully enter into and upon the said premises or any part thereof in the name of the whole and repossess the same and expel the tenant and those claiming under it without being deemed guilty of any manner of trespass and without prejudice to any rights which might otherwise be used for arrears of rent or preceding breach of covenant and upon entry as aforesaid this lease shall determine and the tenant covenants that in case of such termination it will indemnify the landlord against all loss of rent which the landlord may incur by reason of 68
such termination during the residue of the term above specified.

That default provision is in approximately the same language as that which was used in the case of the lease which was used in the action in the United States Supreme Court in the case of *Brown* against *U. S. Trust Company* which was reported in 201 U. S.

Similar forms of the indemnity agreement have also been before the highest Court in this State and other states, and those doctrines agree with the decision of the United States Supreme Court which is to the effect that there is no way of telling 69
until the end of the period of the lease whether or not there will be any loss; that there is no claim, that there is no indebtedness which arises until that period expires.

It is our position—(interrupted by).

The Master: Just a minute. I understood you were making an objection to the introduction. I do not want to argue the law on that because I do not want to pass upon that. I am going to overrule you without passing upon the question of law at all.

70 Mr. Kellogg: I was simply trying to make it clear to your Honor.

The Master: Yes. I know the point you are raising.

Mr. Kellogg: I beg your pardon for elaboration.

The Master: Objection overruled. Exception.

Mr. Glenn: I also offer in evidence, your Honor—(interrupted by).

The Master: Wait a minute. Now you are offering this in evidence?

Mr. Glenn: I offer in evidence Trustee's Exhibit 1 for Identification.

71 (Trustee's Exhibit 1 for Identification is received in evidence and marked, Claimant's Exhibit A, of this date.)

The Master: Let it appear on the record that Mr. Crossman joins in the exception taken by Mr. Kellogg and it is understood that hereafter when any objection is made it is to redound to the benefit of all of the intervenors and that whenever there is any exception every intervenor is to have the benefit of the exception.

Mr. Glenn: I also offer in evidence a second stipulation of facts signed by all interested coun-

72 sel.

The Master: You are going to make objection to that?

Mr. Kellogg: The paper which has just been offered in evidence contains a single provision reserving the right to object to the contents of the paper on the ground that it is immaterial or irrelevant. We object to this entire stipulation on those grounds and those previously stated.

The Master: Objection overruled. Exception to all intervenors. Mark it.

(Document referred to is received in evidence and marked, Claimant's Exhibit B, of this date.) 73

Mr. Glenn: Now I request that the proof of claim filed by these claimants in the old bankruptcy proceeding and your Honor's order allowing the proof of claim in part be deemed to be a part of the records in this proceeding.

(Colloquy off the record.)

The Master: All right, I will so consider them.

Mr. Glenn: In view of the position taken by Mr. Kellogg, I now request your Honor to permit an amendment to the proof of claim filed in these proceedings by the claimants. The amendment reads as follows: 74

"The claimants pray that if the court should determine that their statutory parity claim for three years' rent, etcetera, for injury resulting from the rejection of said lease by the trustee in bankruptcy, or for damages or indemnity under the covenant or covenants contained in said lease, is not presently provable in the above-entitled reorganization proceedings, then and in such event the court should in the order determining that said statutory parity claim is not presently provable provide that said statutory parity claim of 75 the claimants should constitute a legal or equitable charge upon the assets of the debtor payable by the debtor and/or any corporation to which the assets of the debtor may be transferred at such times as the damages suffered by the claimants from said rejection or the breach of said covenants shall become liquidated in accordance with the applicable State law.

"Claimants further pray that if the court should determine that the total amount of damages suffered by the claimants for the entire term of said lease from said rejection or the breach of said

covenants over the amount of said statutory parity claim is not presently provable in the above-entitled reorganization proceedings, then and in such event, whether or not said statutory parity claim shall be held provable at this time, the court should provide in the order so determining that said excess claim should constitute a legal or equitable charge upon the assets of the debtor in subordination to debts which would be provable under Section 63 (a) of the Bankruptcy Act and to any statutory parity claims which may also constitute a charge against said assets, but in priority to the claims or interest of all holders of preferred and common stock of the debtor."

Mr. Kellogg: If your Honor please, we did not know that the claimant was going to ask for an amendment of the proof of claim but it seems to me this is a question of how your Honor might dispose of this thing. The law contains certain provisions as to how certain rights should be reserved, subdivision "h" of Section 77-B. It does not seem to me that it is relevant as an amendment of the claim as it is presented here.

The Master: I do not think it is.

You could raise the issue in your memorandum that you will submit, but I do not think that is a proper amendment of the claim.

Mr. Glenn: Your Honor, the proof of claim is in a sense a pleading in this sort of proceeding. It merely contains one prayer: First, that the court should allow the claim or should, in other words, determine if it is presently provable. It seems appropriate under the circumstances if your Honor should determine that no part of this claim or the excess claim is now presently provable that the status of that claim so far as it can constitute a liability against the debtor should now be determined.

As a matter of fact I should think it would be 79
in the interest of Mr. Kellogg to know at the earliest possible moment what the status of the excess claim is, because until it is determined no plan of reorganization can be negotiated.

Mr. Crossman: I think we do want to know that, whether there is any so-called excess claim.

The Master: If that be so, don't you think it would be wise for you to withdraw your objection to the amendment at this time and have that matter passed on?

Mr. Kellogg: Your Honor, I would prefer that this should be before the Court. I am reading 80
that. I do not see any harm.

Mr. Morgulas: I think that would be a proper amendment.

Mr. Kellogg: As a part of the prayer for relief I will consent to the amendment in that regard.

The Master: All right, mark it.

Mr. Swatland: That means, I take it, consenting to the request for the amendment, not the relief prayed for.

Mr. Crossman: Objecting to the relief prayed for.

The Master: Mark it. 81

(Paper referred to is received in evidence and marked Claimant's Exhibit C of this date.)

The Master: Off the record.

(Further discussion off the record.)

Mr. Glenn: That is the claimant's case, your Honor.

Mr. Kellogg: Pardon me, Mr. Glenn, are you not going to offer in evidence the map which you referred to in the affidavit there?

82 Mr. Glenn: No, I did not think it was necessary, Mr. Kellogg, since the stipulation concedes —(interrupted by).

Mr. Kellogg: Have you that map here?

Mr. Glenn: No, I did not bring it here.

Mr. Kellogg: I thought that would be part of the record here.

Mr. Glenn: It simply goes to establish that the real estate expert there is a real estate expert.

(Further colloquy off the record.)

Mr. Kellogg: Judge Wise.

83 Mr. Crossman: Before you call a witness I want to state that in connection with this claim I reserve my right to object to the constitutionality of that part of 77-B which puts this claim on a parity with claims which originally were provable in bankruptcy.

Mr. Glenn: I would suggest that your Honor deny that request and I think that perhaps Mr. Crossman on second thought may consent to its withdrawal, because it seems to me that question is bound up to some extent with the question which is presented in this claim because we shall argue that if your Honor finds that the claim is
84 not presently provable that the statute is unconstitutional and that the provision according a claim a statutory parity for three years' rent and so forth is unconstitutional, which is really the objective aimed at by Mr. Crossman.

Mr. Crossman: I think the objective, if I may say so—(interrupted by).

The Master: I am going to let him reserve any of his rights.

Mr. Morgulas: I think we have that in the record already.

The Master: Yes.

Mr. Crossman: Off the record. 85

(Further discussion off the record.)

The Master: You have rested as I understand?

Mr. Glenn: Yes, I have rested.

The Master: All right, I will hear the other side.

GEORGE J. WISE, a witness called in behalf of the trustee and intervenors, having been first duly sworn by the Master, testified as follows:

Direct examination by Mr. Kellogg:

86

Q. Judge Wise, you have been since August 29, 1932, an employee of the Irving Trust Company? A. Yes, sir.

Q. First as trustee in bankruptcy and then as trustee in the present proceeding? A. Yes.

Q. In that capacity you have been serving in the real estate department of the trustee? A. Yes.

Q. Prior to that time you had been for a great many years the head of the real estate department of the United Cigar Stores Company of America? A. Yes.

87

Q. The debtor in this proceeding? A. Yes.

Q. You have studied properties in various cities with a view to renting those properties? A. Yes.

Q. On behalf of the United Cigar Stores Company or its trustee? A. Yes.

Q. Are you acquainted with the property which is located at—which is known as the Adam-Fischer Estate property and which is located—which is known as No. 45 East State Street, Trenton, New Jersey? A. Yes.

Q. Will you please state on what—will you

88 please state what the size of Trenton, New Jersey, is? A. I think about 115,000 or 120,000 population.

Q. Does that city have its shopping properties draw upon contiguous territory? A. Yes, very largely.

Q. Where is the center of the City of Trenton? A. State and Broad Streets.

Q. Where is this property with regard to the corner of State and Broad Streets? A. Adjoining one of the corners. I will get the direction in a moment from this map.

89

The Master: When you state the center, Mr. Wise, you mean the shopping center rather than the actual center of the town?

The Witness: I meant the shopping center, the business center.

Q. You were getting the directions. A. Yes. That would be the northwest corner.

Q. This is a location which was formerly occupied by the United Cigar Stores Company or its subsidiary company? A. Yes.

Q. It adjoins the corner property? A. Yes.

90 Q. Which was also occupied by the United Cigar Stores Company or its subsidiary company? A. Yes.

Q. And that adjacent property is known as the Bugbee property? A. Correct.

Q. In determining chain store locations, the best locations as I understand it you refer to as one hundred percent locations? A. Yes.

Q. How would you describe this location here in the parlance of the chain store real estate management? A. Taking the four corners I would say they would represent the business center

of the city and constitute the one hundred percent locations of property for business purposes. 91

Q. Where is the capital of the State of New Jersey located with reference to the property, in which direction? A. To the west.

Q. That is desirable property for the renting to a chain store project like a chain shoe store? A. I would say it is desirable for any retail business.

Q. Is that location going downhill at all at the present time to your knowledge? A. No. I consider it still the center of Trenton.

Q. So far as you can judge in the future it would continue to be one of the best locations in the City of Trenton? A. Yes. 92

Mr. Kellogg: That is all.
The Master: Mr. Glenn?
Mr. Glenn: No questions.
(Thereupon, the witness was excused.)
Mr. Kellogg: Mr. Sientz.

MICHAEL I. SIENTZ, a witness called in behalf of the trustee and intervenors, having been first duly sworn by the Master, testified as follows: 93

The Master: Your full name?
Mr. Sientz: Michael I. Sientz.

Direct examination by Mr. Kellogg:

Q. What is your business? A. Real estate department for the United Cigar Stores, now the Irving Trust Company, trustee.

Q. Prior to the bankruptcy of United Cigar Stores Company on August 29, 1932, you were

94 connected with the United Cigar Stores Company? A. I was.

Q. In the real estate department? A. Yes, sir.

Q. For how long a time had you been connected in that way? A. Thirteen years prior to 1933.

Q. What are your duties or what were your duties for the United Cigar Stores immediately prior to the bankruptcy? A. Securing locations and renewals of leases with landlords.

Q. With the trustee are your duties approximately the same? A. The same thing.

95 Q. Are you acquainted with the property which is referred to as No. 45 East State Street, in the City of Trenton, State of New Jersey? A. I am.

Q. The size of that property is approximately eighteen and a half by sixty-five feet?

The Master: Now just a minute. Off the record.

(Further discussion off the record.)

Mr. Kellogg: Your Honor, a copy of the lease is annexed to the stipulation which has been offered here.

(Further colloquy off the record.)

96 The Master: The next question.

Q. How would you describe this in the parlance as a chain store location, Mr. Sientz? A. I would consider it one of the best corners in the City of Trenton.

Mr. Glenn: May I interrupt, are you putting Mr. Sientz on the stand as a real estate expert?

The Master: Yes, as I understand it.

Mr. Kellogg: I am.

The Master: Frankly, I do not think you ought to spend much time on this, because Mr. Bugbee who is the owner of the other portion of the premises and former comptroller of the State of New Jersey, has been dealing with real estate all his life and his testimony was to the effect that it was the best corner in Trenton. 97

Mr. Kellogg: Of course, that is not in this record, your Honor.

Q. You have heard the testimony of Judge Wise in this proceeding? A. Yes.

98

Mr. Glenn: May I ask a few questions, your Honor?

The Master: Yes.

Cross examination by Mr. Glenn:

Q. I take it that you negotiated the lease with the United on the property known as the Fischer Estate property? A. Not on the Fischer property. I did on the Bugbee property.

Q. Did you ever negotiate leases on any other property in the City of Trenton? A. Yes.

Q. What other leases? A. Those are the only two stores we had in Trenton. 99

Q. Did you ever live in the City of Trenton? A. No, sir, I did not.

Q. What experience other than what has been elicited from you so far have you had in connection with leasing stores for the company? A. I have leased stores for the company in the entire State of New Jersey.

Q. But you know nothing about real estate conditions in Trenton? A. Yes, as far as rental values are concerned.

Michael I. Sientz—for Trustee and Interrenors—By Master.

100

Q. Based upon what experience? A. Checking up other locations.

Q. You mean you go over from New York City? A. From New York City.

Q. And you had actually negotiated in Trenton two leases and that is all? A. That is all in the City of Trenton.

Mr. Glenn: I object to this man as being an expert on real estate values in the City of Trenton.

101 The Master: Objection overruled. He has had considerable experience in the State of New Jersey. I think he is qualified as an expert.

Mr. Glenn: On that basis, your Honor, these people in the United would be experts of real estate all over the country, which is impossible.

The Master: Off the record.

(Further discussion off the record.)

Examination by the Master:

Q. Mr. Sientz, as a matter of fact, as part of
102 your duty you contact other chain store representatives in other lines? A. Yes, sir.

Q. And you are familiar with renting conditions throughout the State of New Jersey? A. Throughout the State of New Jersey and other States.

Q. And the United has other stores in other sections of New Jersey near Trenton? A. Elizabeth, New Brunswick, Summit, Newark, almost every city in the State of New Jersey of any consequence.

Mr. Glenn: I say that is all immaterial, irrelevant, your Honor.

103

The Master: I disagree with you, Mr. Glenn. Objection overruled. Exception.

Re-direct examination by Mr. Kellogg:

Q. Mr. Sientz, before making the lease in the City of Trenton that you refer to, did you canvass the city for locations and ascertain the prices for those locations? A. I tried to check up on other rental values in the city.

Q. Have you recently attempted to check up on rental values? A. The last time I was there was prior to the end of last year.

104

Q. You have contacted, however, real estate men in the City of Trenton so that you have obtained their views as to the real estate rental values in the City? A. In the City of Trenton and elsewhere.

Q. I am not sure whether I asked this question or not: You heard the testimony of Judge Wise? A. I did.

Q. And you agree entirely with his testimony? A. Yes, sir.

Q. As far as you are able to judge at the present time this property is not deteriorating or going downhill? A. Absolutely not.

105

The Master: Cross examination?
Mr. Glenn: I have nothing.
The Master: Off the record.
(Further discussion off the record.)

Examination by Mr. Kellogg (continuing):

Q. Mr. Sientz, will you please tell me whether Trenton is a city of diversified industries or of one interest? A. Diversified industries.

106 Q. What other industries are located there? A. Terra Cotta goods, rubber goods, china, Roebling works—that is a steel works right outside of the city.

Mr. Glenn: Pardon me, your Honor, I fail to see how this witness can testify as to what industries are located in the City of Trenton.

May I ask a question?

The Master: Yes.

107 Cross examination by Mr. Glenn:

Q. Have you actually visited the industrial plants which produce these products in the City of Trenton? A. I don't have to necessarily visit the plants.

Q. Of your own actual knowledge you do not know whether these products are manufactured in the City of Trenton or not? A. I answered that I do know.

Q. How do you know? A. Well, all you have to do is just to go down there by train. You can see them all along the railroad tracks and not very far from the city.

108

Q. By going through by train you can tell what they manufacture? A. Yes, you can see the plants. Or, by driving down by automobile. I believe they have their advertising motto right on it, what they manufacture, the names of the firms.

Q. And that is the basis on which you have testified? A. Yes.

Mr. Glenn: Proceed.

109

Re-direct examination by Mr. Kellogg:

Q. What would you consider that the City of Trenton is particularly noted for in its manufacture? A. China. The Lenox china is manufactured down there.

Q. It is the center of the pottery industry? A. Yes.

Q. Has the City of Trenton suffered more from the present depression than other cities of similar sizes, if you know? A. That is a question I would not know definitely.

110

Q. But you do not know definitely that it has? A. No, I do not.

Mr. Kellogg: That is all.

The Master: Cross examination?

Mr. Glenn: No questions.

The Master: Anything else?

(Thereupon, the witness was excused.)

The Master: The only thing left for me to do is to fix a time for the briefs.

How much time do you want, Mr. Glenn?

111

Mr. Kellogg: We would like quite a little time, your Honor.

(Further discussion off the record.)

The Master: July 8th for Claimant's brief. Is that satisfactory?

Mr. Glenn: Yes.

The Master: How much time do the intervenors and the trustee want? Or, isn't the trustee going to file one in this case?

Mr. Swatland: I think we may.

112 The Master: How much time do you want after the 8th?

Mr. Swatland: I think two weeks.

The Master: All right, is that satisfactory to everybody, July 22nd? (No response.)

July 22nd for reply memoranda; July 26th for answering memoranda; entire matter to be submitted on the 26th at which time you will file your exhibits.

(Further discussion off the record.)

Mr. Tuttle: Your Honor, we would like to file a memorandum in this case.

113 The Master: You can. You are one of the intervenors.

(Thereupon, at 3:25 o'clock, P. M., the hearing was closed.)

114

Claimants' Exhibit A.

115

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor. 116

STIPULATION OF FACTS RELATING TO CLAIM OF CAROLINE R. KUEHNER AND FREDERICK G. FISCHER, AS TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF ADAM FISCHER, DECEASED, AGAINST UNITED CIGAR STORES COMPANY OF AMERICA (No. 5184).

The following facts are agreed to by and between the undersigned in lieu of formal proof thereof:

On October 18, 1926, Edward A. Fischer and 117
Caroline R. Kuehner, as executors of and trustees under the will of Adam Fischer, deceased, were the legal owners in fee of the premises hereinafter referred to, and Edward A. Fischer and Caroline R. Kuehner, individually, and Frederick G. Fischer, Margaret G. Fischer, Margarette Hensler, Louis Fischer, Jr., and Ruth Fischer were the then living beneficiaries of the trust of said premises created under the will of said Adam Fischer, deceased. Said premises were demised under a certain indenture of lease which the aforesaid

118 persons, as landlords, made on October 18, 1926, to United Cigar Stores Company of America, as tenant. The terms and provisions of said lease are set forth in full in Exhibit "A", annexed to this stipulation.

On the 24th day of December, 1933, Edward A. Fischer died, and on April 20, 1934, Frederick G. Fischer was duly appointed and qualified as successor trustee under the last will and testament of Adam Fischer, deceased, in the place and stead of said Edward A. Fischer, deceased. At all times after the 24th day of April, 1934,
119 Caroline R. Kuehner and Frederick G. Fischer, as trustees under the last will and testament of Adam Fischer, deceased, were, and they still are, the legal owners in fee of said premises said legal owners being herein called the "Claimants".

United Cigar Stores Company of America, the corporation which is the Debtor in the above-entitled proceeding for reorganization, hereinafter called the "Debtor", on August 29, 1932, filed its voluntary petition in bankruptcy and was adjudicated a bankrupt in the bankruptcy proceeding initiated thereby (Docket No. 55,129), and Irving Trust Company was appointed trustee in
120 bankruptcy of the Debtor and acted as such trustee in bankruptcy (hereinafter called the "Trustee in Bankruptcy") until June 14, 1934. On June 9, 1934, the Debtor filed its petition for reorganization under Section 77B of the Bankruptcy Act, and on June 14, 1934, the above-mentioned court made its order approving such petition as property filed under said section. On November 14, 1932, the Trustee in Bankruptcy formally rejected the above-mentioned lease and surrendered the premises covered by said lease to the Claimants as landlords. After rejection and surrender of the premises by the Trustee in

Bankruptcy, the Claimants re-entered into and upon the whole of said premises. 121

On or about the 14th day of November, 1932, Charles N. Schragger, a duly licensed real estate broker doing business in the City of Trenton, New Jersey, was authorized and empowered to let said premises, but no person offered to lease said premises except the following, who became tenants of the Claimants at the following times and under the following terms:

A portion of the premises was relet to Sa Lee Shoppe, Inc., on March 1, 1933, under a lease the terms and provisions of which are set forth in full in Exhibit "B", annexed to this stipulation. 122

A portion of the premises was relet to Barney E. Olitsky on July 26, 1933, under a lease the terms and provisions of which are set forth in Exhibit "C", annexed to this stipulation.

A portion of the premises was relet to Charles C. Wacks on July 15, 1934, under a verbal agreement for a month to month tenancy, commencing on July 15, 1934, at the rate of $20.00 per month. 123

A portion of the premises was relet to one Piat (first name unknown) on May 1, 1934, under a verbal agreement for a month to month tenancy, commencing on May 1, 1934, at the rate of $25.00 per month.

A portion of the premises was relet to E. A. Devlin on January 1, 1933, under a verbal agreement for a month to month tenancy, commencing on January 1, 1933, at the rate of $22.50 per month.

Claimants' Exhibit A.

124 No part of the premises has been relet since the aforesaid rejection of said lease, except as aforesaid.

Neither the Debtor nor the Trustee in Bankruptcy nor any other person has paid the rent or any other obligations accruing under said lease dated October 18, 1926, after the 1st day of August, 1932, except as hereinafter mentioned,—that is to say: no instalment of net rent under said lease has been paid since the instalment of rent under said lease due on August 1, 1932; no instalment of taxes has been paid under said
125 lease since the instalment paid on or about June 1, 1932, such instalment being for the first half of the year 1932; no water rents have been paid under said lease since August 29, 1932; and no premiums on the fire insurance required to be maintained by the tenant under the provisions of Article Ninth of said lease dated October 18, 1926, have been paid thereunder since the premium paid for 1932. The last water rents paid by the Debtor covered the year 1932, and the last premium on fire insurance paid by the Debtor covered the year 1932.

The Claimants received dividends amounting to
126 $1,110.34, which were declared in the above-mentioned proceedings in which the Debtor was adjudicated a bankrupt (Docket No. 55,129) on the claim based on said lease filed by them in said bankruptcy proceeding.

The amount received by the claimants from the Trustee in Bankruptcy of the Debtor for the use and occupation of the premises by the Trustee prior to its surrender of the premises upon rejection of said lease is $646.74.

The amount of the taxes levied and assessed against, on or in respect of said premises for

the years 1932, 1933, 1934 and the first half of 1935 is as follows: 127

1932	$3,980.40
1933	$2,907.09
1934	$3,142.80
1935 (first half)	$1,571.00

The amount of water rents paid for or in respect of said premises for the years 1933, 1934 and for a part of 1935 is as follows:

1933	$ 9.93 (premises only
1934	$55.78 partly occupied 128
1935 (to date)	$ 9.93 during 1933.)

The amount of premiums on fire insurance in the amount of $25,000 on the building on said premises, in respect of the years 1932, 1933 and 1934, are as follows:

1932	$159.50
1933	$159.50
1934 ($35,000)	$223.30

The amount received from said new tenant Sa Lee Shoppe, Inc., under said lease dated March 129
1, 1933 (Exhibit "B"), from the date of the commencement of the term of said lease, to wit, April 1, 1933, to date, is $10,125. The amount of the gross sales of said tenant Sa Lee Shoppe, Inc., for the year ending March 31, 1935, was $44,864.33. No rent has to date been received from nor is payable by said tenant Sa Lee Shoppe, Inc., on account of the gross sales clause contained in said lease (Exhibit "B").

The amount received from said new tenant Barney E. Olitsky under said lease dated July

130 26, 1933 (Exhibit "C"), from the date of the commencement of the term of said lease, to wit, October 21, 1933, to date, is $1,200, although $100 more was due and payable by said tenant under the terms and conditions thereof.

The amount received from said new tenant Charles C. Wacks from the date of the commencement of his tenancy on July 15, 1934, to date, is $220, although said tenant agreed to pay a rental of $20.00 per month during the period of his tenancy.

The amount received from said new tenant
131 Piat from the date of the commencement of his tenancy on May 1, 1934, to date, is $325, although said tenant agreed to pay a rental of $25.00 per month during the period of his tenancy.

The amount received from said new tenant E. A. Devlin from the date of the commencement of his tenancy on January 1, 1933, to date, is $652.50, although said tenant agreed to pay a rental of $22.50 per month during the period of his tenancy.

On October 5, 1934, Frederick G. Fischer and Caroline R. Kuehner, individually and as trustees under the last will and testament of Adam
132 Fischer, deceased, and also as duly authorized agents for the ultimate beneficiaries under said Will, filed in the office of Special Master Irwin Kurtz, 15 Park Row, New York City, the proof of claim which is now on file in the office of said Special Master and which has been numbered 5184, and which as such constitutes a part of the record on the claim set forth in said proof of claim.

The Claimants have at no time assigned to any person such claim as they may have against the Debtor as a result of the facts hereinabove set forth.

Claimants' Exhibit A.

This stipulation is made without prejudice to 133
the right of any of the undersigned to object to the admission of this stipulation in whole or in part on the ground that it or any part thereof is irrelevant or immaterial, but all other possible grounds of objection to its admissibility or to the admissibility of any of the facts herein agreed to are hereby waived.

Dated, June 21st, 1935.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders, 134
Protective Committee.

BERLE & BERLE, SHEARMAN & STERLING,
Attorneys for Preferred Stockholders,
Protective Committee.

SULLIVAN & CROMWELL,
Attorneys for United Stores Corporation.

M. CARL LEVINE,
Attorney for Jacob Ruppert
Realty Corporation. 135

CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for the Trustee of the Estate of United Cigar Stores Company of America.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for the Claimants.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Landlords' Protective Committee.

Claimants' Exhibit A.

136

EXHIBIT A.

LEASE TO DEBTOR.

INDENTURE made this 18th day of October, 1926, by and between EDWARD A. FISCHER and CAROLINE R. KUEHNER, individually and as Executors and Trustees of the Estate of Adam Fischer, late of Trenton, in the County of Mercer, State of New Jersey, and FREDERICK G. FISCHER, MARGARET G. FISCHER, MARGARETTE HENSLER, LOUIS FISCHER, JR. and RUTH FISCHER, hereinafter called "Landlords" and UNITED CIGAR STORES COMPANY OF
137 AMERICA, a New Jersey Corporation, having an office at No. 44 West 18th Street, Borough of Manhattan, City and State of New York, hereinafter called "Tenant", WITNESSETH:

That the Landlords for and in consideration of the rent and covenants hereinafter contained on the part of the Tenant to be paid, kept and performed, have demised and leased and do by these presents demise and lease unto the Tenant and the Tenant does hire from the Landlords, that certain piece or parcel of land situate, lying and
138 being in the City of Trenton, County of Mercer and State of New Jersey, known as and by the Street No. 45 East State Street, and being more particularly described as follows:

BEGINNING on the south side of State Street in the said City of Trenton, at the corner of a lot of Joseph G. Brearley and others and running from thence (1) by said lot south seven (7) degrees west sixty-four (64) feet more or less to other land of said Brearley; thence (2) by said land north eighty-eight and a half (88½) degrees West, twenty-one

(21) feet to the lot of William J. Owens; 139
thence (3) by said lot of said Owens, North eleven (11) degrees East, sixty-six (66) feet more or less to State Street; and from thence (4) by said State Street South seventy-nine (79) degrees East, eighteen (18) feet and six (6) inches to the place of Beginning.

TOGETHER WITH the four story building and improvements thereon erected and the appurtenances thereunto appertaining, for a term of years commencing on November 1st, 1926, and expiring on March 31st, 1946, subject to termination as hereinafter provided; YIELDING AND PAYING THEREFOR 140
unto the said Landlords the yearly rental of Ten Thousand Five Hundred Dollars ($10,500.00) for the first ten (10) years of the term, and the yearly rental of Eleven Thousand Five Hundred Dollars ($11,500.00) for the balance of the term, which rental shall be payable in equal monthly payments in advance on the first day of each and every month during the term hereof. The tenant agrees as a convenience to the Landlords, to pay the first two (2) years' rental in the following manner: Four Thousand Two Hundred Sixty-five and 84/100 ($4265.84) upon execution of this lease, 141
receipt of which is hereby acknowledged, and on the first day of each and every month of the first two (2) years of the term hereof the Tenant shall pay to the Landlords the sum of Eight Hundred Seventy-five Dollars ($875.00) less the sum of One Hundred Seventy-seven and 75/100 Dollars ($177.75) and less a sum equal to six per centum (6%) per annum on all unearned prepaid rental.

This lease is made upon the following conditions, all and every one of which the respective parties covenant and agree to and with each other to keep and perform:

142 FIRST: The Tenant shall and will monthly and every month during the said term hereby granted, well and truly pay or cause to be paid unto the Landlords at No. R. F. D. 6 Trenton, N. J., Trenton, New Jersey, or at such other place as they may designate in writing, the said rent hereby reserved upon the days and at the times hereinbefore limited and prescribed for the payment thereof without fraud or delay, and shall and will at its own proper cost and charges pay and discharge as additional rent hereby reserved all taxes and assessments of every nature, kind and de-
143 scription which may be levied or assessed against said property by the City of Trenton, or State of New Jersey, or other Governmental instrumentality, and all water rents, but nothing herein contained shall be deemed or construed to obligate Tenant to pay any income, inheritance or franchise taxes, or taxes other than those imposed directly upon demised premises. The Tenant agrees to pay the taxes semi-annually upon the twenty-fifth days of April and October in each year, and to pay all assessments and water rents that shall be assessed, levied and imposed upon said property and become due and payable during
144 the said term as and when levied and due; provided, however, that the Tenant shall not be required to pay any part of any assessment upon the demised premises which has been levied, assessed, confirmed and/or become a lien prior to date of commencement of term hereof, and that in case of assessments confirmed after date of commencement of term hereof, and which may become a lien during the term herein demised and may be payable (upon application by the Landlords or otherwise) in installments, the Tenant shall only be obligated to pay such installments

as shall fall due during the term of this lease, or 145
if application by the Landlords is necessary under the law to permit of the payment of such assessments in installments and such application has not been made, the Tenant shall in that event only be obligated to pay such part thereof as would equal and represent the installments due thereon during the term herein demised, if the same were so divided and made payable in installments. It is expressly understood and agreed, however, that taxes for the first and last calendar years of the term, shall be apportioned between the parties hereto based upon the period of occupancy by the Tenant hereunder. 146

The Tenant shall have the right to contest or review by legal proceedings or in such other manner as it deems suitable, which proceedings if instituted shall be conducted promptly at its own expense and free of expense to the Landlords (but Landlords covenant and agree to join in such application if required by the laws, requirements, regulations or authorities wherein the premises are located) any taxes, assessments or water rents imposed upon or against the demised premises, and in case any such taxes, assessments or water rates shall as a result of any such pro- 147
ceedings or otherwise, be reduced, cancelled, set aside or to any extent discharged, then upon the determination of such proceedings, the Tenant shall pay the amount that shall be finally assessed or imposed against said premises or be adjudicated to be due and payable on any such disputed or contested items; and shall also have the right to contest any orders or requirements of any governmental authority or otherwise directing or ordering the making of any alterations, repairs or changes to the demised premises, but any such

alterations, repairs and/or changes which may be finally required to be made shall be made by and at the expense of the Tenant; and the Landlords, do hereby make, constitute and appoint the Tenant their true and lawful attorney in fact in their name or in the name of the Tenant as their agent, to file any tax protest or other papers necessary or required in connection with any of the foregoing and at Tenant's cost and expense to take and prosecute any and all proceedings and take advantage of any remedies which in Tenant's opinion shall be necessary and/or proper in relation thereto. The legal proceedings herein referred to shall include appropriate appeals from any judgments, decrees, orders and/or certiorari proceedings and appeals from orders therein but all such legal proceedings shall be begun as reasonably soon as possible after the imposition of any contested lien and shall be prosecuted to final adjudication with all promptness and dispatch.

SECOND: The Tenant covenants and agrees during the term hereby granted, at its own expense, to promptly execute and comply with all laws, rules, orders and regulations of the State, County and Municipal Governments and of any and all their departments and bureaus which may affect or be applicable to the said demised premises and the sidewalks and curbs in front thereof.

THIRD: And the Tenant does hereby covenant with the Landlords that the Tenant, during the said term, will keep the said premises in as good order and repair as when delivered to it, damage by fire or other casualty of happening excepted; and will keep good with glass of the same kind

and quality as that which may be injured or 151
broken, all the glass now or hereafter in the premises, unless the same shall be broken by fire, but provided that in the event that any of said glass shall be broken or damaged by any cause before the commencement of the term herein demised, the same shall be replaced at the expense of the Landlords, and at the expiration of the term the Tenant will remove its goods and effects, and will peaceably yield up to the Landlords the said premises, in as good order and repair as when delivered to it, damage by fire, casualty or act on the part of any Governmental authority, or- 152
dinary wear and tear and damage by the elements excepted.

FOURTH: It is agreed that the Tenant may assign or transfer this lease at any time without the consent of the Landlords, provided there shall be at the time of such assignment no existing default on the part of the Tenant in the performance of any of the matters and things to be performed by it under the terms hereof, provided that the assignee shall expressly and in writing assume and agree to perform the Tenant's liabilities and obligations hereunder and that the Ten- 153
ant shall deliver to the Landlords duplicate original of such instrument of assignment containing an express covenant on the part of the assignee to assume and perform all the liabilities and obligations of the Tenant hereunder: provided further, however, that the Tenant shall at all times and by these presents does guarantee the just and full performance and discharge of all the terms, covenants and obligations of the Tenant hereunder by any such assignee or assignees and shall and does undertake and agree to in-

demnify and save the Landlords harmless from any and all loss or damage which they might otherwise suffer by reason of any failure or default by the said assignee or assignees in the said performance and discharge thereof. The Tenant may sublet the demised premises or any part thereof for any lawful business or purpose.

FIFTH: That during the term the Tenant will not consent that any trade or occupation shall be carried on upon said premises or any use made thereof which shall be unlawful or contrary to any law of the United States, State of New Jersey, or ordinance or by-laws of the City of Trenton, for the time being in force.

SIXTH: The Tenant shall have the right and privilege at its own cost and expense from time to time during the term to make alterations, changes and improvements in and additions to any building and improvement now or hereafter on the land forming part of the demised premises, and to remodel any of such buildings and/or improvements in such manner as it shall deem advisable, and shall have the right and privilege of demolishing in whole or in part the present or any future building, structure or improvement on such land, and if a building is demolished to erect in lieu thereof another building, built of good substantial material, equal in value to the building now erected on land forming part of demised premises; all such alterations, improvements, repairs, remodeling, demolitions and erections to be performed in accordance with all laws, ordinances, statutes and rulings of the City of Trenton and County of Mercer and State of New Jersey applicable thereto. The Landlords do

hereby make, constitute and appoint the Tenant 157
their true and lawful attorney in fact in their name or in the name of the Tenant as their agent, to file, or Tenant may file in its own name, any and all applications, consents and other instruments that may be necessary or required by any and all public or quasi-public authorities permitting and authorizing such alterations, changes, improvements, additions, demolitions and/or erection of any new buildings; and the Landlords covenant and agree if demanded by the Tenant at any time after the execution of this lease to properly execute or cause to be properly executed 158
and deliver to the Tenant any such applications, covenants and/or other instruments hereinbefore referred to.

It is agreed that the Tenant shall have the right, if it so desires, in constructing any new building on land forming part of demised premises, to construct the said new building in such manner that the same may form a part of any building constructed on the adjoining premises and to be used in connection therewith as a single building or block; provided, however, that said building shall be so constructed that at the expiration of the term of this lease, the part or parts thereof 159
located on said premises may, if the Landlords so desire, be separated each from the other by a division or party wall. In case such new building be so constructed in such manner, the Tenant shall, on or before the date of expiration of the term of this lease, if so required by the Landlords by thirty (30) days' prior notice in writing before the end of such term, construct such a division wall of good and durable materials and in a good and workmanlike manner, at its own cost and expense so that the part or parts of said building

160 on said demised premises shall be completely separated from and independent of the wall or walls on adjoining premises.

The Tenant covenants and agrees that if in the making of alterations and changes to building now on demised premises, it shall remove from upper portion of building above street floor, wash-tubs, bathtubs, plumbing, built-in-beds or fixtures, the salvage thereof shall be the property of Landlords.

The Tenant shall also have the right, in making any alterations, changes or improvements to any
161 building forming a part of demised premises, to connect up the same with any adjoining building or buildings and to remove any wall or walls of demised building for that purpose, provided at the expiration of the term of this lease, if the Landlords so require by thirty (30) days' prior notice in writing before the end of term, to restore walls of building to the condition as good as at present, at the expense of the Tenant.

The Tenant covenants and agrees to indemnify, hold harmless and protect the Landlords from and against all claims, demands, fines, liens, suits, judgments, loss and damage of any and every
162 nature, directly or indirectly arising or growing out of the said alterations, changes, improvements, additions, demolitions and/or erection of new building.

Upon the termination of this lease, Tenant agrees, if so required by the Landlords, to restore said building to its present condition and layout in all respects, and particularly to its present condition and layout in so far as accessibility to the upper floors thereof from the street is concerned.

SEVENTH: The Landlords covenant and agree

that the demised premises will be delivered to the Tenant upon the commencement of the term of this lease in good order, repair and condition and free from all tenancies and occupancies, and free from all taxes, assessments, mortgages (excepting as herein otherwise provided) liens and encumbrances whatsoever, and free from all orders and notices of violations of all public and quasi-public authorities and free from complaints and/or reports of violations noticed or existing in or filed with any Federal, State, County or Municipal authorities. 163

EIGHTH: It is agreed that the Lessor may, during the term at reasonable times enter to view the premises and may show the said premises and building to others, and at any time within three months next before expiration of the said term may affix to any suitable part of the said premises a notice for letting or selling the premises, or building, and keep the same affixed without hindrance or molestation. 164

NINTH: The Tenant shall, at its own expense, insure the building forming part of demised premises in the sum of Twenty-five Thousand Dollars ($25,000.00) in a good and reliable insurance company or companies authorized to do business in the State of New Jersey in the name of and for the benefit of Landlords and shall keep the said building so insured during the entire term of this lease, and all premiums upon said insurance policies shall be paid by Tenant and shall be considered as part of the rent hereunder, and all said policies are to be delivered to and remain in the custody of the Landlords; provided, however, that if at any time, by reason of additions, alterations or changes in the present building, or by rea- 165

166. son of the erection of a new building or buildings on the demised premises, the full insurable value thereof shall be such that the sum of Twenty-five Thousand Dollars ($25,000.00) is less than eighty per centum (80%) of said insurable value, then the amount of said insurance so agreed to be kept in force by the Tenant for the benefit of the Landlords, shall be increased so that the said building or buildings on said premises shall at all times be insured in an amount equal to or in excess of eighty per centum (80%) of the full insurable value thereof.

167 In the event that any present or future building erected on the land forming part of demised premises shall be partially damaged by fire or other casualty or happening during the term it shall be restored to its condition immediately prior to such damage with due diligence by Landlords and all insurance moneys collected upon any policies of insurance upon demised premises shall be paid over to Landlords, and the rent and taxes payable by Tenant, until such repairs shall have been made, shall be apportioned in proportion to the part of the building which is still usable.

168 In case any present or future building erected upon the land forming part of demised premises shall be substantially destroyed by fire or other casualty or happening prior to April 1st, 1942, then Landlords shall erect with due diligence a new building upon the land forming part of demised premises substantially similar to the building so destroyed and all insurance moneys collected upon any policies of insurance upon demised premises shall be paid over to the Landlords and any unearned rent and/or taxes paid in advance by Tenant shall be refunded to Tenant. The rent and taxes payable hereunder by Tenant

shall abate pending construction of the new build- 169
ing by Landlords and until the said building is ready for use and occupancy by Tenant.

In case any present or future building erected upon the land forming part of demised premises shall be substantially destroyed by fire or other casualty or happening after March 31st, 1942, this lease shall cease and come to an end as of the date of such destruction and any unearned rent and taxes paid in advance by the Tenant shall be refunded to it.

In the event that any building forming part of demised premises shall be partially damaged or 170
destroyed prior to the beginning of the term hereof, this lease shall not be affected thereby, but the said building shall be restored to its condition immediately prior to such damage or destruction with due diligence by Landlords, and no rental shall be due or payable, nor shall this lease commence until such premises have been properly restored and fitted for use and occupancy by Landlords.

TENTH: Provided also, and these presents are upon this covenant, that if the Tenant does or shall neglect or fail to perform or observe any of the covenants contained in these presents and on 171
its part to be observed and performed for ten (10) days after notice by the Landlords, or if the estate hereby created shall be taken on execution, and such execution shall not be satisfied, cancelled or otherwise removed within thirty (30) days after notice by Landlords, or if the Tenant shall be adjudicated bankrupt or insolvent according to law, or if any assignment of its property shall be made for the benefit of creditors, then and in any of said cases the Landlord lawfully may enter into and upon the said premises or any part thereof in

172 the name of the whole and repossess the same as of the former estate of the Landlords and expel the Tenant and those claiming under and through it and remove its effects (forcibly if necessary), without being deemed guilty of any manner of trespass, and without prejudice to any remedies which might otherwise be used for arrears of rent or preceding breach of covenant, and upon entry as aforesaid this lease shall determine and the Tenant covenants that in case of such termination it will indemnify the Landlords against all loss of rent which the Landlords may incur by reason of
173 such termination, during the residue of the term above specified.

ELEVENTH: It is further covenanted and agreed by and between the parties hereto that during the term of this lease, the Landlords will not sign any petition, consent or other instrument in writing whereby any person or corporation other than the Tenant or those claiming under it, shall directly or indirectly acquire the right to use or occupy any portion of any street or alley upon which said property abuts, or the space above or under the surface thereof, without the written consent of
174 Tenant, but in all cases where by law the consent or petition of the owner of the property in question is required for any public grant or for any public improvements, the consent or petition of the Tenant shall bind the premises and the parties.

TWELFTH: This lease shall be subject and subordinate to any mortgages now or hereafter placed against said premises, which mortgages are not to exceed in the aggregate the principal sum of Thirty-five Thousand Dollars ($35,000.), and the recording of such mortgage or mortgages shall

have preference and precedence and be superior 175
and prior in lien to this lease irrespective of the
date of recording and the Tenant agrees to exe-
cute any instrument without cost which may be
deemed necessary or desirable to further effectuate
the subordination of this lease to any such mort-
gage or mortgages; and it is agreed between the
parties hereto that in the event of any default
by Landlord under the provisions of any such mort-
gage or mortgages or bond or bonds, which it or
they secure, by reason of which a proceeding is
instituted or threatened for the foreclosure of said
mortgage or mortgages, then the Tenant shall 176
have the right and privilege of remedying such de-
fault at the cost and expense of the Landlords, in-
cluding the right to pay any interest or principal
or other sum due thereunder, and also including
the right to the Tenant of procuring a new mort-
gage loan in substitution for any such mortgage
or mortgages, and the Landlord covenants and
agrees upon demand to execute any new bond
and/or mortgage or other papers necessary or
required to effectuate such new mortgage loan or
loans and to repay to the Tenant upon demand
the cost and expense incurred by the Tenant, in-
cluding costs in such foreclosure proceedings and 177
reasonable counsel fees, and reasonable costs, in-
cluding counsel fees of procuring any such sub-
stitute mortgage loan, if necessary, and in addi-
tion to any other rights and remedies which the
Tenant may have at law or in equity, or under
this lease, the Tenant shall likewise have the right
and privilege of reimbursing itself to the extent of
such sums so incurred as aforesaid, out of rentals
then or thereafter falling due hereunder. Land-
lords agree and covenant that in the event they
shall be called upon by Tenant to execute and/or

deliver any new mortgage or mortgages, bond or
178 bonds or papers hereunder, that Landlord will, if required by Tenant or any new mortgagee, have said mortgage, bond or other papers duly executed, acknowledged and delivered by his wife if he at the time shall be married.

THIRTEENTH: All notices required or agreed to be given by either party shall be in writing and given by personal delivery to the Landlords or to one of the executive officers of the Tenant or shall be sent by registered mail addressed to the party intended to be notified at its last known post office address and notice given as aforesaid shall be a
179 sufficient service thereof.

And the said Landlords do covenant that the said Tenant on paying the said yearly rent and performing the covenants aforesaid, shall and may peaceably and quietly have, hold and enjoy the said demised premises for the term aforesaid.

FOURTEENTH: And it is further understood and agreed that the covenants and agreements contained in the foregoing Lease are binding upon the parties hereto and their respective heirs, executors, administrators, successors, legal representatives and assigns.

180 IN WITNESS WHEREOF, the parties hereto have hereunto set their hands and affixed their respective seals the day and year first above written.

In Presence of:

LOUIS RUDNER

EDWARD A. FISCHER (L. S.)
CAROLINE R. KUEHNER (L. S.)
Individually and as Executors and Trustees of the Estate of Adam Fischer, deceased.

FREDERICK G. FISCHER (L. S.)

Claimants' Exhibit A.

As to LOUIS FISCHER, JR.
JOSEPH FISHBERG

181

MARGARET G. FISCHER (L. S.)
MARGARETTE HENSLER (L. S.)
LOUIS L. FISCHER, JR. (L. S.)
LOUIS FISCHER, JR. (L. S.)
RUTH FISCHER (L. S.)

UNITED CIGAR STORES COMPANY
OF AMERICA,
By GEO. J. WISE,
Vice President.
(Seal)

182

W. A. FERGUSON,
Secretary.

The Rider attached hereto as part of Paragraph 6 hereof and on page 9 hereof was annexed hereto prior to the execution of this lease by any of the parties thereto.

EDWARD A. FISCHER,
CAROLINE R. KUEHNER,
Individually and as Executors and Trustees of the Estate of Adam Fischer, deceased.

183

UNITED CIGAR STORES COMPANY
OF AMERICA,
By GEO. J. WISE,
Vice President.

(Acknowledgments.)

Claimants' Exhibit A.

184 EXHIBIT "B".

THIS INDENTURE, made this 1st day of March, 1933, between,

EDWARD A. FISCHER AND CAROLINE R. KUHNER, Executors of the Estate of Adam Fischer, party of the first part, hereinafter called the Lessor, and

SA LEE SHOPPE, INC., a corporation organized and existing under and by virtue of the laws of the State of New Jersey, having its principal office in the City of Newark, County of Essex
185 and State of New Jersey, party of the second part, hereinafter called the Lessee.

WITNESSETH that the party of the first part in consideration of the rent, conditions, covenants and agreements hereinafter provided for on the part of the party of the second part to be paid, kept and performed, does hereby lease unto the said lessee, the ground floor premises, measuring approximately 50'x18'4" from the window backs and basement located at #45 East State Street, in the City of Trenton, County of Mercer and State of New Jersey, said storeroom to be according
186 to the plans and specifications herewith attached and made part of this lease for the term of five years from April 1st, 1933 to April 1st, 1938.

During the term of this lease the Lessee shall pay to the Lessor a rental, as provided, in the next succeeding paragraph hereof, of eight per cent. (8%) of the gross sales made at the said demised premises during the year from April 1st, to April 1st.

To this end the Lessee shall, within the first ten (10) days of each month, send to the Lessor

a statement in writing, signed in the name of the 187
Lessee, by its President, vice-president, Treasurer or Secretary, which statement shows said gross sales in the demised premises.

The Lessee hereby agrees to guarantee to the Lessor under the term of this lease, a rental of not less than $4500.00 per annum, payable monthly at the rate of $375.00, payable on the first day of each month for the current month in advance, and agrees at the end of each three months' period, beginning as of April 1st, 1933, to calculate the rent due the Lessor for the next preceding three months' period under the terms of 188
this lease at the rate of 8% of the gross sales for the said three months' period and deducting the amount of rent as paid under the minimum guarantee herein provided for and paying on the 10th of the next month thereafter the difference which shall have been earned as rent according to such calculation. It being the intention of the parties hereto that the rental for the premises herein demised shall be at the rate of 8% of the gross sales for an entire year during the term of this lease but the Lessee guarantees a minimum rental of $4500.00 per annum, payable $375.00 per month, in advance. At the expiration of each 189
12 month period, during the terms of this lease, the gross sales will be computed and the amount to be paid is at the rate of 8%. Adjustments for the entire year, in accordance with the above to be made each twelve months' period commencing April 1st, 1934.

The Lessor agrees to install a front and make improvements according to the attached plans and specifications at their own cost and expense and agree to give possession of the herein leased

190 premises on or before March 20th, 1933, in a finished condition ready for occupancy by the Lessee.

The said Lessee accepts this lease upon the following covenants, agreements, conditions and limitations, all and every one of which the said Lessee hereby expressly covenants and agrees to keep, observe and perform.

1. The Lessee agrees to permit the Lessor or the Lessor's representative to enter the herein leased premises and examine the Lessee's books at any reasonable time.

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2. The Lessee shall and will, during the said term promptly pay to the Lessor the rent, herein reserved on the days herein prescribed for the payment thereof.

3. The said premises shall be used and occupied for the sale of women's inside and outside apparel of every description excluding shoes and including women's dresses, women's coats, millinery, hosiery, underwear, lingerie, novelty jewelry and allied articles.

192 The Lessor agrees not to permit any of the remaining space in the building of which the herein leased premises form a part to be used for the sale of any of the above mentioned articles or billiard parlor, bowling alley or men's social club.

4. The Lessee shall not assign, let or underlease the within demised premises without first obtaining the written consent and approbation of the Lessor herein.

Claimants' Exhibit A.

5. The Lessee shall take good care of the premises hereby leased, and shall at its own cost and expense make inside repairs to the herein leased premises, except such as may be necessitated by fire and structural repairs; and at the end or other expiration of the term of this lease will peaceably and quietly leave, surrender and yield up the said premises unto the said Lessor in good order and condition, reasonable use and wear thereof and damages by the elements excepted. 193

6. In case of fire the said Lessee agrees to give immediate notice thereof to the Lessor and in case the building erected on the premises hereby leased shall be partially damaged by fire, the same shall be repaired as speedily as possible at the expense of the Lessor and the rent adjusted equitably for partial damage creating untenantable, portion; in case the damage shall be so extensive as to render the building untenantable, the rent shall cease until such time as the building shall be put in complete repair, but in case of the total destruction of the premises by fire or otherwise, the rent shall be due up to the time of such destruction and then, from thenceforth this lease shall cease and come to an end. 194 195

7. It is expressly understood and agreed that in case the demised premises shall be deserted or vacated, while the rent is unpaid, or if default be made in the payment of the rent for any part thereof as herein specified, or if default be made in the performance of any of the covenants and agreements in this lease, contained on the part of the Lessee to be kept, or if the Lessee shall fail to comply with any of the statutes, ordinances, rules, order, regulations and requirements of the

196 Federal, State and City Government or of any and all their Departments and Bureaus applicable as to its occupancy of said premises, or be adjudicated a bankrupt or make an assignment for the benefit of creditors or take advantage of any insolvency act, and the rent not paid promptly thereafter, terminate this lease and the term thereof, by giving to the Lessee ten (10) days' notice in writing of its intention so to do, and upon the giving of such notice, this lease and the term thereof shall terminate, expire and come to an end on the date fixed in such notice, as if said
197 date were the date originally fixed in this lease for the termination or expiration thereof.

8. The Lessor or agents or representatives of the Lessor shall have the right to enter in and upon said premises with reasonable frequency and at reasonable hours of the day during said term to ascertain if said premises are kept in proper repair and condition.

9. The failure of the Lessor to insist upon a strict performance of any of the terms, conditions and covenants herein shall not be deemed
198 a waiver of any rights or remedies that the landlord may have and shall not be deemed a waiver of any subsequent breach or default in the terms, conditions and covenants herein contained.

10. The Lessee hereby agrees to carry Plate Glass insurance on the herein leased premises at its own cost and expense.

11. Upon the expiration of this lease, or the abandonment of the premises by the Lessee, the Lessor may enter and take possession of the said

premises and remove all person or persons there- 199
from, without being liable therefor to any person.

12. The Lessee may erect signs on the herein leased premises provided said signs conform to all Federal, State and City Regulations.

13. The Lessor hereby agrees to furnish adequate heat for the herein leased premises as required during the term of this lease at their own expense and the Lessee hereby grants permission to the Lessor to take whatever necessary space is required in the basement to install a heating apparatus, and the Lessee hereby agrees to permit 200
the Lessor or their representatives to have egress and exit to the heating apparatus through the basement only.

The Lessor hereby recognizes Chas. N. Schragger, a licensed broker of the State of New Jersey, as the broker in this lease and agrees to pay him 2% of all the rentals paid the Lessor by the Lessee, in the following manner:

> 2% of the total minimum guarantee for the period of the lease at the execution of this lease and 2% of all additional rentals 201
> paid by the Lessee to the Lessor at the time of such payments.

The Lessor agrees also to pay commission to Chas. N. Schragger, the broker on any renewals that the Lessee may take after the termination of this lease.

IN WITNESS WHEREOF, the party of the first part has hereunto set their hands and seals and the party of the second part has hereunto caused these presents to be signed by its president and

202 attested by its secretary and its corporate seal affixed hereto all on the day and year first above written.

EDWARD A. FISCHER L. S.

CAROLINE R. KUEHNER, L. S.
Executors for the Estate of Adam Fischer.

SA LEE SHOPPE, INC.,
LOUIS S. ROSEN, President.

Signed, sealed and delivered
in the presence of
203
CHAS. N. SCHRAGGER.

Attest:

LENA R. ROSEN,
Secretary.

(Seal)

State of New Jersey,
County of —ss.:

BE IT REMEMBERED that on this 1st day of March, 1933, before me, the subscriber, a Notary
204 Public of N. J., personally appeared, Edward A. Fischer and Caroline R. Kuehner who I am satisfied are the persons named in and who executed the foregoing lease and I having first made known to them the contents thereof, they did each acknowledge that they signed, sealed and delivered the same as their voluntary act and deed, for the uses and purposes therein expressed.

CHARLES N. SCHRAGGER,
Notary Public of N. J.
My commission Exp. Apr. 1936.

Claimants' Exhibit A.

State of New Jersey,
County of Essex—ss.: 205

BE IT REMEMBERED, that on this 1st day of March, 1933, before me, the subscriber, an Attorney at Law of New Jersey, personally appeared Lena R. Rosen, who being by me duly sworn on her oath, says that she is the secretary of the Sa Lee Shoppe, Inc., named in the within instrument; that Louis S. Rosen is the President of said corporation; that deponent well knows the corporate seal of said corporation; and the seal affixed to said instrument is such corporate seal and was thereto affixed and said Instrument signed and delivered by said President, as and for his voluntary act and deed and as and for the voluntary act and deed of said corporation, in presence of deponent, who thereupon subscribed her name thereto as witness. 206

LENA R. ROSEN, Secy.

Sworn and subscribed to before me this
1st day of March, 1933.

ABRAHAM I. MAYER,
An Attorney at Law of New Jersey. 207

Claimants' Exhibit A.

208 EXHIBIT "C"

THIS INDENTURE, made the twenty-sixth day of July, One Thousand Nine Hundred thirty-three, Between EDWARD A. FISCHER & CAROLINE R. KUEHNER, Executors of the Est. of ADAM FISCHER, of the City of Trenton, County of Mercer and State of New Jersey, party of the FIRST PART, and Barney E. Olitsky, of Trenton, N. J., party of the SECOND PART, WITNESSETH, that the said party of the first part have let and by these presents do grant, demise, and to farm let, unto the said party of the Second Part, the entire second floor, situated
209 in the property known as 45 East State Street, Trenton, N. J., with the appurtenances, for the term of Five Years from the twenty-first day of October, One Thousand Nine Hundred thirty-three, at the yearly Rent or Sum of Seven Hundred Eighty ($780.00) to be paid in equal monthly payments of sixty-five dollars, in advance.

And it is agreed that if any rent shall be due and unpaid, or if default shall be made in any of the covenants herein contained, then it shall be lawful for the said party of the first part to re-enter the said premises, and to remove all per-
210 sons therefrom. And the said party of the second part does covenant to pay to the said party of the first part, the said yearly rent as herein specified.

The party of the first part at their own cost and expense agrees to do the following: Install transoms in the windows on the second floor premises. Install base plug electrical out-lets as agreed upon. Install three lavatories and toilet where agreed upon. Install gas outlet where agreed upon. Grant the privilege of hanging two Neon signs on the outside of the building. To

grant to the party of the second part the privilege 211
of subletting part of his space. The party of the first part furnishes heat at their own cost and expense during the months that heat is required. And he, the said Barney Olitsky, his executors and administrators, shall and will not, at any time during the said term, let or demise, or in any manner dispose of the hereby demised premises, or any part thereof, for all or any part of the term hereby granted, to any person or persons whatever, nor occupy or use the same in any other manner than as a Dentist's office, Optometrist's office, and general office purposes, without 212
the consent and approbation, in writing, of the said EDWARD A. FISCHER & CAROLINE R. KUEHNER, Executors of the Est. of Adam Fischer, their heirs and assigns, first had for that purpose: And that at the expiration of the said term, the said party of the second part, will quit and surrender the premises hereby demised, in as good state and condition as reasonable use and wear thereof will permit, damages by the elements excepted. And the said party of the first part do covenant that the said party of the second part, on paying the said yearly rent, and performing the covenants aforesaid, shall and may peaceably and quietly 213
have, hold and enjoy the said demised premises for the term aforesaid, and hereby grant to the party of the second part the privilege of erecting such partitions as he may deem necessary, also the privilege of moving in when necessary alterations are completed. Receipt of the sum of $65.00 is acknowledged by the party of the first part from the party of the second part as rent from October 21st to November 21st, 1933.

IN WITNESS WHEREOF, the parties hereto have

214 hereunto set their hands and seals on the day and year first above written.

EDWARD A. FISCHER & CAROLINE R. KUEHNER
Executors of the Est. of Adam Fischer.

EDWARD A. FISCHER (L. S.)
CAROLINE R. KUEHNER (L. S.)
BARNEY E. OLITSKY (L. S.)

Witness:

MAURICE D. SANDLER.

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215 **Claimants' Exhibit B.**

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter

of

216 UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

SUPPLEMENTAL STIPULATION OF FACTS RELATING TO CLAIM OF CAROLINE R. KUEHNER AND FREDERICK G. FISCHER, AS TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF ADAM FISCHER, DECEASED, AGAINST UNITED CIGAR STORES COMPANY OF AMERICA (No. 5184).

IT IS HEREBY STIPULATED AND AGREED by and between the undersigned, that CHARLES N.

Claimants' Exhibit B.

SCHRAGGERG, a real estate appraiser doing business 217
in the City of Trenton, State of New Jersey, is a duly qualified expert on rental values of real estate in the City of Trenton, New Jersey, and particularly real estate situated in the portion of said city in which the premises covered by the lease hereinafter mentioned are situated, and that if called as an expert witness at the hearing to be held before Hon. Irwin Kurtz, as Special Master in the above-entitled proceeding, on the objections to the claim of Caroline R. Kuehner and Frederick G. Fischer, as Trustees under the last will and testament of Adam Fischer, deceased, 218
against the above named Debtor, he would testify as follows:

The fair rental value as of August 29, 1932, of the premises covered by the lease dated October 18, 1926, made by Caroline R. Kuehner and Edward A. Fischer, as Executors of and Trustees under the last will and testament of Adam Fischer, deceased, and others, as landlords, to the Debtor, as tenant, for a term commencing on August 29, 1932, and ending on March 31, 1946, under a lease containing the same provisions as those contained in said lease dated October 18, 1926, except as to the term 219
of the leasehold, is $4,750 a year net. The fair rental value of said premises as of August 29, 1932, for a term commencing November 14, 1932, and ending on March 31, 1946, under a lease containing the same provisions as those contained in said lease dated October 18, 1926, except as to the term of the leasehold, is the same, to wit, $4,750 a year net.

The fair rental value as of November 14, 1932, of said premises for a term commencing on November 14, 1932, and ending on March 31, 1946, under a lease containing the same provisions

as those contained in said lease dated October 18, 1926, except as to the term of the leasehold, is also $4,750 a year net.

That in his judgment there is no substantial difference in the rental values of said premises whether taken as of August 29, 1932, or November 14, 1932, as during this period there was no appreciable change in rental values.

The aforesaid opinion as to the rental value of said premises is based not only upon the change in rental values since the lease between the landlords and the Debtor dated October 18, 1926, was made and August 29, 1932 and November 14, 1932, respectively, but also upon the factor that said premises must now be rented as an inside property separate and apart from the adjoining premises situated on the corner of State and Broad Streets, Trenton, New Jersey, whereas both said premises and said corner premises were rented as a unit to the Debtor by the respective owners thereof on or about October 18, 1926. Said corner premises were relet as a separate unit, under a lease negotiated by Charles N. Schragger, for a term of ten years; that, accordingly, in his opinion there will be no possibility whatever of reletting during said ten-year period the premises covered by the lease dated October 18, 1926, in conjunction with said corner premises.

That the present return from the premises in question is only a net amount of $3,000 a year, but that over the period of approximately fourteen (14) years said premises should return a net annual rental, as previously stated, of $4,750.

This stipulation is made without prejudice to the right of any of the undersigned to object to the admission of this stipulation in whole or

in part on the ground that it or any part thereof 223
is irrelevant or immaterial, but all other possible grounds of objection to its admissibility or to the admissibility of any of the facts herein agreed to, or to the qualification of said witness as an expert witness to give opinion evidence, are hereby waived.

Dated, June 21st, 1935.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders' Protective Committee. 224

BERLE & BERLE, SHEARMAN & STERLING,
Attorneys for Preferred Stockholders' Protective Committee.

SULLIVAN & CROMWELL,
Attorneys for United States Corporation.

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corporation.
225

CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for the Trustee of the Estate of United Cigar Stores Company of America.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for the Claimants.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Landlords' Protective Committee.

Claimants' Exhibit C.

AMENDMENT TO PROOF OF CLAIM ON BEHALF OF FISCHER ESTATE.

226 The claimants pray that if the court should determine that their statutory parity claim for three years' rent, etc., for injury resulting from the rejection of said lease by the Trustee in Bankruptcy, or for damages or indemnity under the covenant or covenants contained in said lease, is not presently provable in the above-entitled reorganization proceedings, then and in such event the court should in the order determining that said statutory parity claim is not presently provable provide that said statutory parity claim of
227 the claimants should constitute a legal or equitable charge upon the assets of the Debtor payable by the Debtor and/or any corporation to which the assets of the Debtor may be transferred at such times as the damages suffered by the claimants from said rejection or the breach of said covenants shall become liquidated in accordance with the applicable state law.

Claimants further pray that if the court should determine that the total amount of damages suffered by the claimants for the entire term of said lease from said rejection or the breach of said covenants over the amount of said statutory
228 parity claim is not presently provable in the above-entitled reorganization proceedings, then and in such event, whether or not said statutory parity claim shall be held provable at this time, the court should provide in the order so determining that said excess claim should constitute a legal or equitable charge upon the assets of the Debtor in subordination to debts which would be provable under Section 63 (a) of the Bankruptcy Act and to any statutory parity claims which may also constitute a charge against said assets, but in priority to the claims or interests of all holders of preferred and common stock of the Debtor.

Notice of Making and Entry of Report of Special Master.

229

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

230

Sirs:

PLEASE TAKE NOTICE that the within is a true copy of a report made and entered herein by Hon. Irwin Kurtz, Special Master, on Oct. 23, 1935.

Dated, New York, N. Y., October 25th, 1935.

Yours, etc.,

CRAVATH, DE GERSDORFF,
SWAINE & WOOD,
Attorneys and Solicitors for Irving Trust Company, Trustee of the estate of United Cigar Stores Company of America, Debtor,
Office and Post Office Address,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

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To:

HARVEY T. SATTERTHWAITE, ESQ.,
Attorney for Caroline B. Kuehner and Frederick G. Fischer, etc.,
137 E. State Street,
Trenton, New Jersey.

Notice of Making and Entry of Report of Special Master.

ROSENBERG, GOLDMARK & COLIN,
165 Broadway,
New York, N. Y.
Attorneys for Debtor.

M. CARL LEVINE,
535 Fifth Avenue,
New York, N. Y.
Attorney for Jacob Ruppert Realty Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
20 Exchange Place,
New York, N. Y.

and

RALPH MONTGOMERY ARKUSH,
15 Broad Street,
New York, N. Y.
Attorneys for Landlords' Protective Committee.

SHEARMAN & STERLING,
55 Wall Street,
New York, N. Y.

and

BERLE & BERLE,
70 Pine Street,
New York, N. Y.
Attorneys for Preferred Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
15 Broad Street,
New York, N. Y.
Attorneys for Debentureholders Protective Committee.

SULLIVAN & CROMWELL,
48 Wall Street,
New York, N. Y.
Attorneys for United Stores Corporation.

Report of Special Master.

UNITED STATES DISTRICT COURT, 235

SOUTHERN DISTRICT OF NEW YORK.

No. 59,886.

In proceedings for reorganization of a corporation.

Claim No. 5184.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor. 236

To the Honorable Judges of the United States District Court, Southern District of New York:

I, IRWIN KURTZ, Special Master herein, do hereby respectfully report, as follows:

This is an application to expunge the claim of Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, Landlords, for damages based 237 upon a covenant of indemnity contained in the lease herein. The Bondholders Protective Committee and the Preferred Stockholders Committee, Intervenors, contend that the Landlords are not entitled to any allowance at this time, but that pursuant to the terms of the covenant of indemnity, that the damages, if any, must only be allowed after March 31, 1946, the expiration date of the lease herein. The Claimants and counsel for the Jacob Ruppert Realty Corporation—Landlord Intervenor—contend that the

238 Landlords herein are entitled to an immediate allowance for all damages sustained for the balance of the term.

The situation presented herein is as follows: Heretofore and on the 18th day of October, 1926, the Landlords and the United Cigar Stores Company of America (United) entered into a lease for the premises herein situate in the City of Trenton, New Jersey, for a term commencing November 1st, 1926 and expiring on March 31st, 1946, at the yearly rental of Ten thousand ($10,000) Dollars the first ten years, and Eleven
239 thousand ($11,000) Dollars for the balance of the term. Paragraph 10th thereof, among other things, provided that in the event of the Tenant's default, insolvency, or bankruptcy, that the Landlords could enter into possession of the premises without prejudice to any remedies for arrears of rent or preceding breach of the covenant, and that

> "upon entry, as aforesaid, this lease shall determine and the tenant covenants that in case of such termination, it will indemnify the landlords against loss of rent which the
> 240 landlords may incur by reason of said termination, during the residue of the term above specified".

Pursuant to the terms of the lease, the United entered into possession of the premises and continued to occupy same. On August 29th, 1932 it filed its voluntary petition and was adjudicated a Bankrupt, on that day, and the Irving Trust Company was appointed Receiver. On September 10, 1932 the Irving Trust Company was elected Trustee. Thereafter and on November

14, 1932 the Irving Trust Company as Trustee 241
in Bankruptcy formally rejected the lease herein and surrendered to the Landlords possession of the premises. The Landlords thereupon re-entered upon the premises and thereafter let portions thereof for various terms. Based upon the foregoing, and irrespective as to the terms of the covenant of indemnity herein, the Landlords in view of the law as to claims for future rent in bankruptcy had no provable claim in the prior United bankruptcy proceeding.

However, on June 7th, 1934 Congress enacted 242
Section 77B of the Bankruptcy Act. Thereupon on June 9th, 1934 the United filed its petition for reorganization, which was duly approved, and the Irving Trust Company was appointed as Trustee in Reorganization. Based upon Section 77B, subd. (b) which provides in part, as follows:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this Section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, 243
> in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, for its acceptance and confirmation, be deemed to be a creditor. The claim of a Landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease, shall be treated as a claim ranking on a parity with debts which would be provable

244 under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the above surrender of the premises to the landlord or the date of reentry of the landlord, which ever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry:"

the Landlords filed the instant claim for damages
245 for $90,212.90 for breach of its covenant of indemnity caused by the rejection of the lease by the Trustee as aforesaid. The Landlords claimed $45,049.95 as their damages for the three years in accordance with the specific provisions of said Section 77B, subd. (b). As to the damage in excess thereof, the Landlords claimed that the amount thereof should be allowed in subordination to debts provable in bankruptcy, but in priority to the interests of the stockholders of the United.

Upon the hearing, the Trustee conceded that the Landlords were entitled to damages to the extent of the amount of rent reserved for three years,
246 but it objected to any allowance in excess thereof upon the ground that there was no provision in Section 77B therefor. The Bondholders Committee and the Preferred Stockholders Committee, as Intervenors, however, objected to the allowance of the Landlords' claims in any amount upon the ground that it could not now be determined whether the Claimants would suffer any loss as the result of the breach of the covenant of indemnity, and urged that this question could only be determined at the expiration of the term pursuant to the rule enunciated in *Hermitage v. Levine*, 248 N. Y. 233.

The Stockholders Protective Committee joined 247
in the objection made by the Trustee, namely, that as a matter of law the Landlords did not have any claim under Section 77B in excess of the three year period provided for. Thereupon, proof was adduced as to the reasonable rental value of the premises for the entire balance of the term, and the legal question herein was presented for determination.

The objecting Intervenors argue that at common law, upon the covenant herein, the Landlords could not bring an action until the expiration of the term, relying upon the rule in *Hermitage* v. 248
Levine (248 N. Y. 233) (*supra*). This proposition of law is not disputed. It is equally true as stated heretofore that the Landlords had no provable claim for damages in bankruptcy. The Landlords, however, point out that we are not now concerned with proceedings at common law or with provable claims in the ordinary bankruptcy proceedings;—that we are presently confronted with rights asserted by the Landlords under Section 77B. They contend that the question before the Court is the interpretation of the rights granted to Landlords under a 77B proceeding. They argue that when the purpose of the 249
enactment of Section 77B is considered, when an examination of the provisions thereof is made, and the intent of Congress ascertained, that it will become apparent that the Landlords' claim herein not only for the three years but in excess thereof, should be allowed in all respects.

There is no need of dwelling upon the purposes of the enactment of Section 77B. They are well-known and have repeatedly been set forth by the Courts. The entire aim of Section 77B was to attain results absolutely opposite to that usually

obtained in a bankruptcy proceeding. Suffice it to say that with its broad scope of conservation of business, and to furnish the assistance required by the inroads made by the depression, necessary provision had to be made that a reorganization should include every possible claim existing against the Debtor—whether it was absolute, conditional, contingent, or otherwise. There could not be any distinction between provable or non-provable claims, as existed in the ordinary bankruptcy liquidation proceeding. Accordingly, Congress took the pains to state (Sec. 77B, subd. (b)) that

> "The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interest of whatever character."

Obviously, a Landlord whose lease had been rejected by a Trustee and the premises returned, had a claim under Section 77B, for damages where the lease contained a covenant of indemnity.

That such a Landlord could not maintain an action at common law upon its indemnity covenant until the expiration of the term made no difference to the aims and purposes of Section 77B, and the results that were sought to be obtained therefrom. The fact remained that such

a Landlord had a claim under this Section, and 253
that it necessarily would have to be included in
and disposed of in a reorganization proceeding.

It must be borne in mind that we are not presently dealing with actions at common law where the only parties involved are the Landlord and the Tenant. We are now administering a Statutory system with a definite goal. As the Supreme Court said in *William Filene's Sons Co.* v. *Weed*, 245 U. S. 597—"When a statutory system is administered, the only question for the Courts is what the statutes prescribe".

Thus, if we merely considered the purposes of 254
Section 77B, with its all inclusive definition of "claims" and "creditors", the Landlord's claim herein would have to be allowed to the extent of the damages that could be legally provable. However, Section 77B gives further proof that Congress intended to make a claim of this nature provable herein. In addition to the endeavor to accomplish the beneficent purposes of reorganization, Congress was confronted with the problem caused by the non-provability of Landlord claims for future rent, particularly after the decision of the United States Supreme Court in the *Manhattan Properties-Irving Trust Company*, 291 U. 255
S. 320.

Congress realized the situation produced by the bankruptcies of many chain stores, followed thereafter by the rejection of leases by the Trustee in Bankruptcy, resulting in the losses sustained by Landlords. Congress was aware of the distinctions attempted to be drawn in the usual bankruptcy proceedings, based upon the language of the leases—whether contained in covenants of indemnity or otherwise, such as ipso facto provisions, for penalties, for presently measuring

256 damages, or for indemnity provisions accruing at the end of the term, for options to re-enter by the Landlords and other similar conditions. It was to obviate the very results of the Landlord situation in bankruptcy proceedings, that Congress made additional and specific provision in Section 77B for Landlords, where there was an unexpired lease and the same had been rejected either by a Trustee in Bankruptcy or by direction of the Court.

Congress by the enactment of Section 77B, subdivision (b) did not merely say that upon re-
257 jection of an unexpired lease that a Landlord should have a claim for damages. Congress in order to avoid any misunderstanding as to the scope of its enactments, specifically enumerated, and made such a Landlord's claim all embracing and inclusive and specifically provided not only for all injury resulting from such rejections but also "for damages or for indemnity under a covenant or covenants contained in the lease". No limitation was placed upon such a Landlord's claim. Obviously, the intent was to grant a landlord a right to an immediate allowance in a reorganization proceeding, where there had been
258 a rejection of his unexpired lease, irrespective as to whether his rights were based upon a covenant of damages or a covenant of indemnity with a clause for immediate assessment of damages or at the expiration of the term, and irrespective whether an action could be maintained immediately at common law upon any such covenant of indemnity.

It was also Congress' intent to free a Debtor of all future liability on executory contract of indemnity by proceedings in reorganization where there had been a rejection of the lease, as afore-

said, either by a Trustee or pursuant to an order 259
of the Court. The purpose was to effect a present, immediate disposition and adjustment of all claims actual or contingent, and to fix the present value of the contract or the amount of the damage suffered as a result of such rejection of the unexpired lease by the Trustee in Bankruptcy or by order of the Court, so as to efficiently and expeditiously aid and carry through the purposes of reorganization.

Undoubtedly Congress could under its broad bankruptcy powers set up this system of reorganization, could make provision that all claims should 260
be included and bound by such a proceeding, could furnish additional remedies—whether by anticipatory breach or otherwise—to a Landlord with an indemnity clause as in the instant case, where the Trustee in Bankruptcy had rejected the lease, and to make provision in the Statute as to the method and manner of proving a Landlord's damages in a reorganization proceeding. Obviously, Congress had the right to create such a remedy, as part of its plan of reorganization and the distribution of a Debtor's assets.

A claim based upon the indemnity covenant 261
herein can be evaluated in a Section 77B proceeding. It is reasonably susceptible of immediate valuation. Loss of rents over a period of time in the future can be presently ascertained, and this is determined by the difference between the rent reserved and the rental value for the balance of the term. The United States Supreme Court in *William Filene's Sons Co.* v. *Weed,* 245 U. S. 597, stated this method to be "upon a footing that was familiar and fair".

In view of all the foregoing the Landlord's claim herein should be allowed as provided in

262 Section 77B to the extent of three years' rent on an equal parity with other provable claims. Such an allowance will carry out the laudable purposes sought to be accomplished by the Reorganization Act. This is eminently just and proper, and is in accordance with the express provisions of Section 77B (subd. (b)), as specifically pointed out heretofore.

Whether the Landlords are entitled to an allowance in excess of the three years' period, in subordination to the provable claims, but in priority to stockholders, is not required to be determined at this time. Whether there will be a
263 surplus over and above the amount of provable claims and expenses of administration, how the same is to be distributed and, in fact, the method of payment and manner thereof to the various creditors, will depend upon the classification of creditors and the respective rights of the various interested parties herein. All these matters will only be presented when the time for classification arrives, and when various questions arise in the consideration and the confirmation of any Plan of Reorganization. Accordingly I will adopt the suggestion of the Trustee and the opposing Inter-
264 venors, and will leave the question as to the allowance of any excess claim for future consideration, as aforesaid.

After the hearings had been concluded, and briefs submitted, my attention was called to the Report of Hon. Thomas D. Thatcher, acting as Special Master, in the Matter of Radio Keith Orpheum Corp., Debtor. Permission was afforded to the parties to serve additional briefs based upon their contentions in respect thereto. I have carefully examined this Report and I find that it

does not affect the legal question presented herein. 265
It appears therefrom as follows:

(a) *In re claim of Rockefeller Center, Inc.*—the Special Master recognized Section 77B did not limit merely to a three year period basis a liquidated damage claim which would have been provable in a bankruptcy proceeding for a period beyond three years, and that the purpose of this section was to provide for landlords' claims which heretofore were not provable in a bankruptcy proceeding. He also applied the general rule that damages cannot be awarded upon a 266
claim which is so indefinite, so uncertain and so speculative as to be incapable of proof, when it appeared that certain office space was surrendered, and the tenant in November 1932, agreed that at the Landlord's option to lease five years later, namely, December 1937, such part thereof as would not be then leased by the Landlord—it thus appearing that neither the obligation nor the damage for the breach of this supplemental agreement could be foretold.

(b) *In re claims of Hoblitzlle*, the Special 267
Master stated the well-established rule that the debtor's liability as a guarantor of various leases based upon covenants as to the reletting of the premises and holding the tenant for a deficiency is non-existent until a deficiency is ascertained; and that accordingly a claim upon such guaranty with respect to future rents is so far contingent as not to be susceptible of proof. (It should be noted herein that these claims were all founded upon a guaranty; and that they were not based upon any of the provisions

268 of §77B, as there had been no rejections of the leases by a Trustee in Bankruptcy or by an order of the Court.)

(c) In the claim of Broadway & 47th Street Corp., Landlord, the Special Master specifically pointed out that it was clearly distinguishable from the instant case. Both the covenant of indemnity contained therein as well as in the Landlords' lease herein, made no provision for the immediate assessment of damages, measured by the difference between the rental value and the
269 rent reserved for the balance of the term. Accordingly, neither landlord pursuant to the rule of *Hermitage* v. *Levine, supra,* could have maintained an action at common law until the expiration of the term; and of course, neither landlord had a provable claim in bankruptcy. However, at this point the similarity between the two situations ceases. Broadway & 47th Street Corp., landlord, had no claim in a §77B proceeding for the very good reason that there was no rejection of an unexpired lease by the Trustee in Bankruptcy or by an order of the Court, and ac-
270 cordingly its claim was not based on the specific provisions of Section 77B, subd. (b). The Special Master points to this fact on page 41 of his Report, as follows:

> "It is further contended in behalf of the claimant that subdivision (b) of Section 77-B, the Corporate Reorganization section of the Bankruptcy Act, authorizes the allowance of its claim for the difference between the rent reserved and the rental value of the premises, limited to an amount not to exceed the rent without ac-

celeration reserved by the lease for the 271
three years next succeeding the date of surrender. In this case there was no rejection of the lease by any trustee or receiver in bankruptcy or in equity, or pursuant to any direction of a judge in this proceeding. The premises were surrendered by the assignee of the debtor corporation pursuant to the notice given by the landlord under the Twenty-first article of the lease." * * * (Underscoring mine.)

However, in the instant case the Irving Trust Company as Trustee in Bankruptcy herein, did 272
on November 14th, 1932 reject the lease and did surrender to the Landlords possession of the premises which was followed by the Landlords' re-entry upon the premises. Accordingly, the Landlords herein base their claim solely on the rights conferred on them by the specific provisions of Section 77B, subd. (b).

(d) In the Fort Worth Properties claim, the Special Master based his decision upon the termination of the lease by the Landlord prior to any rejection by the Trustee and therefore not upon any claim asserted under 273
Section 77B, subd. (b), as aforesaid.

The Special Master in his Report suggests that contingent claims "incapable of proof"—such as was presented in the surrendered office space in the Rockefeller Centre claim—should be left to the Court for equitable treatment in any Plan of Reorganization. However, as to contingent claims that "are capable of proof"—(other than the instant case, based specifically upon the indemnity clause of Section 77B subd. (b) *supra*)—he recommends that the ascertainable damages to the last day of the filing of claims should

only be allowed, and the balance of the claim should be left to the Court for equitable treatment in any Plan of Reorganization.

However, such a rule may not be of general application. My experience has shown that there is no hard and fast rule as to the time limit within which proofs of claim must be filed in a reorganization proceeding. An examination of the records in the Clerk's office in this District will indicate that claims have been required to be filed as early as within thirty days after the approval of the petition in reorganization. In fact, I have had a proceeding in which claims were not required to be filed until after the confirmation of the Plan, and the claims were to be allowed upon the basis of the records of the Debtor and with adjustments to be made thereafter.

Thus, it may not be practicable or feasible to split up such claims in two periods—(1) up to the date of the filing of the claims which may be very close to the date of the approval of the petition of reorganization, and (2) at the time of the consideration of the Plan of Reorganization. It seems to me that where there is a legal method of ascertaining damages such as taking the difference between the rent reserved and the reasonable rental value, that damages should be assessed at one time upon the hearing held upon the objection to the claim, disposed of then, and the amount of the Debtor's obligations immediately ascertained. This would indeed accomplish the very purposes and come within the scope contemplated by Section 77B. Such a rule would be workable, feasible, and of general application.

However, as pointed out heretofore, the Special Master's Report in the Radio Keith Orpheum Corp. is not applicable to the situation herein

presented. The decisions on the claims in his Report have no bearing either upon the facts or upon the questions of law involved in this case. Accordingly, the recommendations in said Report as to the treatment of unprovable contingent claims, and as to the splitting up of the damages of contingent claims, which are capable of proof (and which are not founded specifically upon the indemnity clause of §77B, subd. (b) caused by a rejection of the lease by a Trustee or by order of the Court, as aforesaid), likewise have no relevancy or bearing upon the legal question presented herein. 277

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From the evidence adduced upon the hearing had herein, it is conceded by the Irving Trust Company, as Trustee, that the total damage which the Landlords herein would suffer as the result of the aforesaid rejection over the term of their lease which expires on March 31st, 1946, will not be less than the three year period specifically set forth in Section 77B, sub. (b) and allowable on an equal parity with other provable claims in bankruptcy. This amounts to $44,377.55.

Accordingly, I recommend that the Landlords should be allowed the said sum of $44,377.55 as a general claim, and that all questions as to the excess of their claim—namely, beyond the statutory three year period—should be reserved until the time of the classification of creditors and stockholders according to the nature of their respective claims and interests, and the consideration of a plan of reorganization, as aforesaid. 279

Respectfully submitted,

IRWIN KURTZ,
Special Master.

Dated, New York, October 23, 1935.

Exceptions of Claimants to Report of Special Master.

280

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter

of

281

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

EXCEPTIONS OF CAROLINE R. KUEHNER AND FREDERICK G. FISCHER, AS TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF ADAM FISCHER, DECEASED, TO REPORT OF HON. IRWIN KURTZ, SPECIAL MASTER, DATED OCTOBER 23, 1935, RELATING TO CLAIM NO. 5184.

282 Now come Caroline R. Kuehner and Frederick G. Fischer, as trustees under the last will and testament of Adam Fischer, deceased (hereinafter called the "Claimants"), and respectfully except to the report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935, as follows:

1. To so much of said report as determines that the question whether the claim of the Claimants is entitled to be allowed in an amount in excess of the amount of the rent for three years in subordination to provable claims but in priority to the interests of all stockholders is not

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now presented and will only be presented "when the time for classification arrives, and when various questions arise in the consideration and the confirmation of any Plan of Reorganization".

2. To so much of said report as determines that the question whether there will be a surplus in excess of the amount of provable claims and expenses of administration depends, or will depend, on "the classification of creditors and the respective rights of various interested parties herein", and to so much of said report as impliedly determines that the question of the validity of the claim of the Claimants in excess of the amount of the rent for three years need not be determined until it is determined whether there is a surplus of assets in excess of the amount of provable claims and expenses of administration.

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3. To so much of said report as asserts that the Trustee and opposing intervenors suggested to the Special Master that the question as to the allowance of the claim of the Claimants in excess of the amount of the rent for three years should be reserved for future consideration.

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4. To so much of said report as determines that the question whether the claim of the Claimants should be allowed in excess of the amount of the rent for three years in subordination to provable claims but in priority to the interests of all stockholders, is not required to be determined at this time.

5. To so much of said report as determines that the question "as to the excess of their [the Claimants'] claim—namely, beyond the statutory

286 three-year period—should be reserved until the time of the classification of creditors and stockholders according to the nature of their respective claims and interests, and the consideration of a plan of reorganization".

6. To said report in so far as it fails to determine that the amount of the claim of the Claimants in excess of the sum of $44,377.55, the amount of the statutory three-year claim, is provable and allowable in subordination to other provable claims but in priority to the interests of all stock-
287 holders.

7. To said report in so far as it fails to determine the amount of the claim of the Claimants in excess of the sum of $44,377.55, the amount of the statutory three-year claim.

8. To said report in so far as it fails to determine that if the amount of the claim of the Claimants in excess of the sum of $44,377.55, the amount of the statutory three-year claim, is not provable and allowable, it remains a charge upon the assets of the Debtor or any corporation to which the assets of the Debtor may be transferred, in pri-
288 ority to the interests of all stockholders.

9. To said report in so far as it fails to determine that, if the amount of the claim of the Claimants in excess of the sum of $44,377.55, the amount of the statutory three-year claim, is not provable and allowable, the statute does not extinguish or destroy said excess portion of the claim.

10. To said report in so far as it fails to determine that, if the statute, properly construed, provides that if said excess claim of the Claimants

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is not provable and allowable and does not remain a charge upon the assets of the Debtor in priority to the interests of all stockholders, the provision or provisions of Section 77B so providing and extinguishing the claim are unconstitutional as beyond the power conferred upon the Congress by the bankruptcy clause of the Constitution (Article I, Section 8, Clause 4), and as violative of the Fifth Amendment of the Constitution in that it deprives the Claimants of property without due process of law and takes their property for public use without just compensation.

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11. To said report in so far as it fails to determine that, after eliminating such unconstitutional parts of the statute, the claim of the Claimants is, under the statute, provable and entitled to participate in any plan of reorganization herein in full on a parity with all other provable claims.

12. To said report in so far as it fails to determine that the claim of the Claimants herein is provable and allowable and entitled to participate in any plan of reorganization herein in full on a parity with all other provable claims.

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Dated, November 4, 1935.

Respectfully submitted,

CAROLINE R. KUEHNER and
FREDERICK G. FISCHER,
as trustees as aforesaid,

By MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys and Solicitors for the
Claimants,
Office and Post Office Address,
20 Exchange Place,
New York, N. Y.

Exceptions of Preferred Stockholders' Protective Committee to Report of Special Master.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

EXCEPTIONS OF PREFERRED STOCKHOLDERS' PROTECTIVE COMMITTEE OF UNITED CIGAR STORES COMPANY OF AMERICA, INTERVENORS HEREIN, TO REPORT OF HONORABLE IRWIN KURTZ, SPECIAL MASTER, DATED OCTOBER 23, 1935, IN RESPECT TO CLAIM OF FREDERICK G. FISCHER AND CAROLINE R. KUEHNER, AS TRUSTEES, ETC. CLAIM NO. 5184 AND TO THE RULINGS OF THE SAID SPECIAL MASTER AT THE HEARING THEREON.

To the Honorable Judges of the United States District Court, for the Southern District of New York:

Now, come Grayson M.-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Protective Stockholders' Protective Committee of United Cigar Stores Company of America, Intervenors herein, and respectfully except to the

Exceptions of Preferred Stockholders' Protective Committee to Report of Special Master.

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Report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935, recommending that the claim of Frederick G. Fischer and Caroline R. Kuehner, as executors and trustees under the will of Adam Fischer (Claim No. 5184) be allowed as a general claim herein in the amount of $44,377.55, and to the rulings of the said Special Master at the hearing thereon, as follows:

1. To so much of such report as refers

(a) To the purposes of the enactment of Section 77B of the Bankruptcy Act,

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(b) To the alleged circumstance that a reorganization under Section 77B should include every possible claim existing against the Debtor, whether such claim be absolute, conditional, contingent or otherwise,

(c) To the alleged circumstance that there can be no distinction under Section 77B between provable and non-provable claims, as existed in the ordinary bankruptcy liquidation proceeding,

as having any bearing on the legal questions presented by the claim herein or the objections made thereto.

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2. To so much of said report as decides that a landlord whose lease has been rejected by a Trustee and the premises returned has a claim under Section 77B for damages where the lease contains a covenant of indemnity.

3. To so much of said report as decides that the fact that such a landlord as the present claimants could not maintain an action at common law

298 upon the indemnity covenant contained in the lease until the expiration of the term makes no difference to the aims and purposes of Section 77B and the results that were sought to be obtained therefrom, and that such a landlord has a claim under Section 77B which would necessarily have to be included in and disposed of in a reorganization proceeding.

4. To so much of said report as determines that a consideration of the purposes of Section 77B and any of the language of Section 77B re-
299 quires that the landlords' claim herein be allowed to the extent of the damages that could be legally provable.

5. To so much of said report as determines that the intent of Congress in the enactment of Section 77B was to grant a landlord a right to an immediate allowance in a reorganization proceeding, where there had been a rejection of his unexpired lease, irrespective as to whether his rights were based upon a covenant of damages or a covenant of indemnity with a clause for immediate assess-
300 ment of damages or at the expiration of the term, and irrespective as to whether an action could be maintained immediately at common law upon any such covenant of indemnity.

6. To so much of said report as refers

(a) To the alleged intent of Congress to free a debtor of all future liability on executory contracts of indemnity by proceedings in reorganization where there has been a rejection of the lease either by a Trustee or pursuant to an order of the Court,

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(b) To the alleged purpose of Congress to effect a present immediate disposition and adjustment of all claims, actual or contingent, and to fix the present value of the contract or the amount of the damage suffered as a result of such rejection of the unexpired lease by the Trustee in Bankruptcy or by order of the Court, so as to efficiently and expeditiously aid and carry through the purposes of reorganization,

as having any bearing on the legal questions presented by the claim herein or the objections made 302
thereto.

7. To so much of said report as determines that a claim based upon the covenant of indemnity contained in the lease upon which the claim herein is based can be evaluated in a Section 77B proceeding and is reasonably susceptible of immediate valuation, and that loss of rents over a period of time in the future can be presently ascertained by the difference between the rent reserved and the rental value for the balance of the term, or in any other manner. 303

8. To so much of said report as determines that the landlords' claim herein should be allowed to the extent of three years' rent on an equal parity with other provable claims, and that such an allowance will carry out the purposes sought to be accomplished by Section 77B, is just and proper, and is in accordance with the express provisions of Section 77B, subdivision (b).

9. To so much of such report as fails to determine that the amount of the claim, if provable or

304 allowable, should be limited to an amount not to exceed the rent, without acceleration, reserved by the lease for the three years next succeeding the date of surrender of the premises to the claimants or the date of reentry of the claimants, whichever first occurred, plus unpaid rent accrued up to such date of surrender or reentry.

10. To so much of such report as decides that it is not required at the present time to determine whether landlords are entitled to an allowance in excess of the three years' period in subordination
305 to the provable claims, but in priority to stockholders and as decides that the method of distribution of the surplus over and above the amount of provable claims and expenses of administration, the method of payment and manner thereof will depend upon the classification of creditors and the respective rights of the various interested parties and as decides that such matters shall only be presented when the time for classification arises and when the various questions arise in the consideration and confirmation of any Plan of Reorganization.

306 11. To so much of said report as determines that the Report of the Hon. Thomas D. Thacher, acting as Special Master in the matter of Radio Keith-Orpheum Corporation, Debtor, does not affect or is not applicable to the legal questions presented by the claim herein and the objections made thereto, and to so much of such report as attempts to distinguish said Report of said Hon. Thomas D. Thacher as such Special Master, or any portion thereof, on any grounds mentioned in the report of the Hon. Irwin Kurtz, dated October 23, 1935, or otherwise.

Exceptions of Preferred Stockholders' Protective Committee to Report of Special Master.

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12. To so much of such report as refers to the time limit within which proofs of claim must be filed in a reorganization proceeding as having any bearing on the legal questions presented by the claim herein and the objections made thereto.

13. To so much of said report as recommends that damages measured by the difference between the rent reserved and the reasonable rental value should be assessed upon the hearing held upon the objection to the claim, disposed of then, and the amount of the Debtor's obligations immediately determined, and that such a rule would accomplish the purposes and come within the scope contemplated by Section 77B and would be workable, feasible, and of general application.

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14. To so much of such report as recommends that the landlords herein should be allowed the sum of $44,377.55 as a general claim herein.

15. To such report in whole and in each and every part thereof for the determination therein that an order should be made herein directing the allowance of said claim in said sum of $44,377.55, or in any other amount, as a general claim against the estate of the Debtor herein.

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16. To such report in whole and in each and every part thereof for failure to determine that an order should be entered herein disallowing said claim in whole as a general claim against the estate of the Debtor herein and barring said claim from participation in any plan of reorganization proposed or confirmed herein on a parity with other claims allowed or allowable as general claims herein.

Exceptions of Preferred Stockholders' Protective Committee to Report of Special Master.

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17. To the ruling of the Special Master at the hearing on the claim in admitting evidence as to the rental value of the demised premises on or about August 29, 1932.

18. To the ruling of the Special Master at the hearing on the claim in admitting the evidence as to the rental value of the demised premises on or about November 14, 1932.

The foregoing exceptions are submitted as both general and specific exceptions and are intended to apply to such report and all findings and determinations therein and all rulings at the hearing on the claim which are inconsistent with such exceptions.

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Dated November 4, 1935.

Respectfully submitted,

SHEARMAN & STERLING,

and

BERLE & BERLE,

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Attorneys for Preferred Stockholders' Protective Committee.

Exceptions of Debentureholders' Protective Committee to Report of Special Master. 313

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA, 314
Debtor.

EXCEPTIONS OF DEBENTUREHOLDERS' PROTECTIVE COMMITTEE TO REPORT OF HONORABLE IRWIN KURTZ DATED OCTOBER 23, 1935, IN RESPECT TO CLAIM OF FREDERICK G. FISCHER AND CAROLINE R. KUEHNER, AS TRUSTEES, ETC. CLAIM NO. 5184.

To the Honorable Judges of the United States District Court for the Southern District of New York: 315

Now, come Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, by their attorneys, Davis, Polk, Wardwell, Gardiner & Reed, and respectfully except to the Report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935, recommending that the claim of Frederick G. Fischer and Caroline R. Kuehner, as executors and trustees under the will of Adam Fischer (Claim No. 5184) be al-

Exceptions of Debentureholders' Protective Committee to Report of Special Master.

316 lowed as a general claim herein in the amount of $14,377.55, as follows:

1. To so much of such report as refers

(a) To the purposes of the enactment of Section 77B of the Bankruptcy Act,

(b) To the alleged circumstance that a reorganization under Section 77B should include every possible claim existing against the Debtor, whether such claim be absolute, conditional, contingent or otherwise,

317 (c) To the alleged circumstance that there can be no distinction under Section 77B between provable and non-provable claims, as existed in the ordinary bankruptcy liquidation proceeding,

as having any bearing on the legal questions presented by the claim herein or the objections made thereto.

2. To so much of said report as decides that a landlord whose lease has been rejected by a Trustee and the premises returned has a claim under 318 Section 77B for damages where the lease contains a covenant of indemnity.

3. To so much of said report as decides that the fact that such a landlord as the present claimants could not maintain an action at common law upon the indemnity covenant contained in the lease until the expiration of the term makes no difference to the aims and purposes of Section 77B and the results that were sought to be obtained therefrom, and that such a landlord has a claim under Section 77B which would necessarily have

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to be included in and disposed of in a reorganization proceeding.

4. To so much of said report as determines that a consideration of the purposes of Section 77B and any of the language of Section 77B requires that the landlords' claim herein be allowed to the extent of the damages that could be legally provable.

5. To so much of said report as determines that the intent of Congress in the enactment of Section 77B was to grant a landlord a right to an 320
immediate allowance in a reorganization proceeding, where there had been a rejection of his unexpired lease, irrespective as to whether his rights were based upon a covenant of damages or a covenant of indemnity with a clause for immediate assessment of damages or at the expiration of the term, and irrespective of whether an action could be maintained immediately at common law upon any such covenant of indemnity.

6. To so much of said report as refers

(a) To the alleged intent of Congress to 321
free a debtor of all future liability on executory contracts of indemnity by proceedings in reorganization where there has been a rejection of the lease either by a Trustee or pursuant to an order of the Court.

(b) To the alleged purpose of Congress to effect a present immediate disposition and adjustment of all claims, actual or contingent, and to fix the present value of the contract or the amount of the damage suffered as a result of such rejection of the unexpired lease

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by the Trustee in bankruptcy or by order of the Court, so as to efficiently and expeditiously aid and carry through the purposes of reorganization,

as having any bearing on the legal questions presented by the claim herein or the objections made thereto.

7. To so much of said report as determines that a claim based upon the covenant of indemnity contained in the lease upon which the claim here-
323 in is based can be evaluated in a Section 77B proceeding and is reasonably susceptible of immediate valuation, and that loss of rents over a period of time in the future can be presently ascertained by the difference between the rent reserved and the rental value for the balance of the term, or in any other manner.

8. To so much of said report as determines that the landlords' claim herein should be allowed to the extent of three years' rent on an equal parity with other provable claims, and that such an al-
324 lowance will carry out the purposes sought to be accomplished by Section 77B, is just and proper, and is in accordance with the express provisions of Section 77B, subdivision (b).

9. To so much of said report as determines that the Report of the Hon. Thomas D. Thacher, acting as Special Master in the Matter of Radio Keith-Orpheum Corporation, Debtor, does not affect or is not applicable to the legal questions presented by the claim herein and the objections made thereto, and to so much of such report as

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attempts to distinguish said Report of said Hon. Thomas D. Thacher as such Special Master, or any portion thereof, on any grounds mentioned in the report of the Hon. Irwin Kurtz, dated October 23, 1935, or otherwise.

10. To so much of such report as refers to the time limit within which proofs of claim must be filed in a reorganization proceeding as having any bearing on the legal questions presented by the claim herein and the objections made thereto.

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11. To so much of said report as recommends that damages measured by the difference between the rent reserved and the reasonable rental value should be assessed upon the hearing held upon the objection to the claim, disposed of then, and the amount of the Debtor's obligations immediately determined, and that such a rule would accomplish the purposes and come within the scope contemplated by Section 77B and would be workable, feasible, and of general application.

12. To so much of such report as recommends that the landlords herein should be allowed the sum of $44,377.55 as a general claim herein. 327

13. To such report in whole and in each and every part thereof for the determination therein that an order should be made herein directing the allowance of said claim in said sum of $44,377.55, or in any other amount, as a general claim against the estate of the Debtor herein.

14. To such report in whole and in each and every part thereof for failure to determine that an order should be entered herein disallowing said

328 claim in whole as a general claim against the estate of the Debtor herein and barring said claim from participation in any plan of reorganization proposed or confirmed herein on a parity with other claims allowed or allowable as general claims herein.

The foregoing exceptions are submitted as both general and specific exceptions and are intended to apply to such report and all findings and determinations therein which are inconsistent with such exceptions.

329 In making the foregoing exceptions the said Debentureholders' Protective Committee expressly reserves its rights to object to the constitutionality of that portion of Section 77B of the Bankruptcy Act which purports to establish the claim herein on a parity with claims which were originally provable against the bankrupt estate of the Debtor herein.

Dated, November 2, 1935.

Respectfully submitted,

330 DAVIS, POLK, WARDWELL,
GARDINER & REED,
Attorneys for Debentureholders'
Protective Committee.
Office and Post Office Address,
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

To:

ROSENBERG, GOLDMARK & COLIN,
165 Broadway,
New York, N. Y.
Attorneys for Debtor.

Exceptions of Debenturcholders' Protective Committee to Report of Special Master.

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M. CARL LEVINE,
535 Fifth Avenue,
New York, N. Y.
Attorney for Jacob Ruppert Realty Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
20 Exchange Place,
New York, N. Y.,

and

RALPH MONTGOMERY ARKUSH,
15 Broad Street,
New York, N. Y.
Attorneys for Landlords' Protective Committee.

332

SHEARMAN & STERLING,
55 Wall Street,
New York, N. Y.,

and

BERLE & BERLE,
70 Pine Street,
New York, N. Y.
Attorneys for Preferred Stockholders' Protective Committee.

333

SULLIVAN & CROMWELL,
48 Wall Street,
New York, N. Y.
Attorneys for United Stores Corporation.

CRAVATH, DE GERSDORFF, SWAINE & WOOD,
15 Broad Street,
New York, N. Y.
Attorneys and Solicitors for Irving Trust Company, Trustee of the Estate of United Cigar Stores Company of America, Debtor.

Certificate of Special Master to District Court.

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UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59,886.

In the Matter

of

335 UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

To the Honorable Judges of the United States District Court, Southern District of New York:

I, IRWIN KURTZ, Special Master herein, make the following report:

1. On October 23, 1935 I made a Report
336 recommending that the claim of Frederick G. Fischer and Caroline R. Kuehner, as executors and trustees under the will of Adam Fischer, Landlords, for damages based upon a covenant of indemnity contained in a lease herein, should be allowed in the sum of $44,377.55, as a general claim, and that all questions as to the excess of the Landlords' claim herein—namely beyond the statutory three year period—should be reserved until the time of the classification of creditors and stockholders according to the nature of their

respective claims and interests, and the consideration of a Plan of Reorganization. 337

2. On November 4th, 1935, the Landlord-Claimants herein and two of the intervenors, namely, the Bondholders Protective Committee and the Preferred Stockholders Committee, feeling aggrieved thereat filed exceptions.

3. The exceptions urged by the Bondholders Protective Committee and by the Preferred Stockholders Committee, briefly summarized, are that pursuant to the terms of the covenant of indemnity herein, that the Landlord-Claimants have 338 no presently allowable claim but their damages, if any, must be ascertained at the expiration of the lease, namely, March 31st, 1946; the Preferred Stockholders Committee also urge in their exceptions that in any event the said Landlord-Claimants have no claim in excess of the statutory three year period provided for by Section 77B. On the other hand, the Claimant-Landlords contend in their Exceptions that they are presently entitled to an allowance beyond the three year parity period, namely, damages for the entire period of the lease. 339

4. The respective contentions of the Trustees, the Claimant-Landlords and the Intervenors, as well as the legal questions involved herein, are fully set forth in the Special Master's Report dated October 23rd, 1935, to which this Court is respectfully referred.

5. I hand up herewith the following:

(a) Exceptions.

(b) Special Master's Report.

340 (c) Objections and application to expunge.

(d) Stenographic minutes and exhibits.

Dated, New York, November 6th, 1935.

.....

Special Master.

This Certificate will be placed on the Bankruptcy Motion Calendar in the District Court, on Wednesday November 13th, 1935 at 10:30 A. M.

341 Notice thereof by mail given to:

CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for Trustee,
15 Broad Street,
N. Y. C.

ROSENBERG, GOLDMARK & COLIN,
Attorneys for Debtor,
165 Broadway,
N. Y. C.

342 M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corporation,
535 5th Avenue,
N. Y. C.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Claimants and Landlords Protective Committee,
20 Exchange Place,
N. Y. C.

RALPH MONTGOMERY ARKUSH, 343
Attorneys for Landlords Protective
Committee,
15 Broad Street,
N. Y. C.

SHEARMAN & STERLING,
Attorneys for Preferred Stockholders
Protective Committee,
55 Wall Street,
N. Y. C.

BERLE & BERLE, 344
Attorneys for Preferred Stockholders
Protective Committee,
70 Pine Street,
N. Y. C.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debenture Holders Protective
Committee,
15 Broad Street,
N. Y. C.

SULLIVAN & CROMWELL,
Attorneys for United Stores Corporation
and for Debtor in State Court Actions, 345
48 Wall Street,
N. Y. C.

Order Appealed From.

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At a Special Term for Bankruptcy Motions of the United States District Court in and for the Southern District of New York, at the Court House thereof, Foley Square, the Borough of Manhattan, City and Southern District of New York on the 4th day of February, 1936.

Present—HONORABLE JOHN C. KNOX,
United States District Judge.

347 In Proceedings for Reorganization of a Corporation—No. 59886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
a New Jersey corporation,

Debtor.

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348 On reading and filing the report, dated October 23, 1935, of Honorable Irwin Kurtz, Special Master, recommending that the claim filed herein by Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer (hereinafter called the claimants) be allowed in the principal amount of $44,377.53 as a general claim on an equal parity with other provable claims, and that all questions as to the excess amount claimed by such claimants in subordination to provable claims against the Debtor, but in priority to the interests of the holders of

the Preferred and the Common stock of the 349
Debtor, be reserved until the time of the classification of creditors and stockholders of the Debtor for the purposes of a plan of reorganization; and

Upon the exceptions to said report, dated November 2, 1935, and filed herein on behalf of the Debentureholders Protective Committee, the exceptions dated November 4, 1935, and filed herein on behalf of the Preferred Stockholders Protective Committee, and the exceptions dated November 5, 1935, and filed herein on behalf of the claimants; the certificate of the Special Master, dated November 6, 1935, certifying to this Court the questions 350
presented by such exceptions, and upon the other documents and papers referred to in said certificate, and after hearing M. Carl Levine, Esq., attorney for Jacob Ruppert Realty Corporation, in support of said report in its entirety, Messrs. Mitchell, Taylor, Capron & Marsh, attorneys for the claimants, by Henry L. Glenn of counsel, in support of said report, except in so far as it reserved the question of the status of the excess claim above referred to, and Messrs. Davis, Polk, Wardwell, Gardiner & Reed, attorneys for the Debentureholders Protective Committee, by Ralph M. Carson, Esq., and Messrs. Shearman & Sterling 351
and Messrs. Berle & Berle, attorneys for the Preferred Stockholders Protective Committee, by Winthrop H. Kellogg of counsel, both in opposition to said report, and after due consideration, it is, on motion of Cravath, de Gersdorff, Swaine & Wood, attorneys for the Trustee of the Debtor's Estate,

ORDERED that the report of Honorable Irwin Kurtz, Special Master, dated October 23, 1935, with respect to the claim of Frederick G. Fischer and Caroline R. Kuehner, as Executors and

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Trustees under the Will of Adam Fischer, be, and the same is, approved and confirmed, with the exception that the extent of the claimants' right to participate in these proceedings shall be limited to the amount found by said report to be allowable, to-wit, $44,377.55.

JNO. C. KNOX,
U. S. D. J.

Filed 2/5/36.

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353 **Claimants' Petition for Appeal and Order Allowing Appeal.**

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation.

No. 59,886.

In the Matter

of

354 UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

To the Honorable the Judges of the District Court of the United States, Southern District of New York:

The petitioners, Caroline R. Kuehner and Frederick G. Fischer, as trustees under the last will and testament of Adam Fischer, feeling them-

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selves aggrieved, for the reasons set forth in the assignment of errors hereto annexed and filed herewith, by the order of this Court dated February 4, 1936, and entered herein on or about February 5, 1936, approving and confirming the report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935, in so far as said report recommended the allowance of the claim of said petitioners against United Cigar Stores Company of America, the Debtor herein, in the amount of $44,377.55, as a general claim on an equal parity with other provable claims, and otherwise dis- 356
approving said report and limiting the right of said petitioners to participate in the above-entitled proceedings to said amount of $44,377.55 and extinguishing the claim of said petitioners to the extent that the amount thereof exceeds the sum of $44,377.55, hereby appeal to the United States Circuit Court of Appeals for the Second Circuit from so much of said order as extinguishes the portion of the claim filed by said petitioners herein in excess of the amount of $44,377.55 and limits the right of said petitioners to participate in the above-entitled proceedings to said amount, and pray that their appeal be al- 357
lowed and that a citation issue, as provided by law, directed to all of the parties to the above-entitled proceedings, commanding them to appear before said United States Circuit Court of Appeals to do and receive what may pertain to justice to be done in the premises, and that a transcript of the record upon which said order dated February 4, 1936, was based and of all proceedings relating to said claim, duly authenticated, be transmitted to said United States Circuit Court of Appeals, and that a proper order re-

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lating to the security to be required of the appellants be made, and for such other and further relief as to this Court may seem just and proper in the premises.

Dated, New York, N. Y., March 3, 1936.

CAROLINE R. KUEHNER and
FREDERICK G. FISCHER,
as trustees under the will of
Adam Fischer,

By MITCHELL, TAYLOR, CAPRON
& MARSH,

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Attorneys and Solicitors for
Caroline R. Kuehner and Frederick G. Fischer, as trustees
under the will of Adam
Fischer,

Office and Post Office Address,
20 Exchange Place,
New York, N. Y.

360

Claimants' Petition for Appeal and Order Allowing Appeal.

361

United States of America,
Southern District of New York,
County of New York—ss.:

HENRY L. GLENN, being duly sworn, deposes and says: That he is associated with the firm of Mitchell, Taylor, Capron & Marsh, attorneys and solicitors for Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, the petitioners named in the foregoing petition; that he has read the said petition and knows the contents thereof; that the same is true to his own knowledge, except as to the matters therein stated to be alleged on information and belief, and as to those matters, he believes it to be true.

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HENRY L. GLENN.

Sworn to before me this
3rd day of March, 1936.

THOMAS I. FITZGERALD,
Notary Public,
New York County.
N. Y. Co. Clk's No. 107, Reg. No. 7F321.
Commission expires March 30, 1937.

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ORDERED that the foregoing petition is granted, appeal is allowed as prayed for and bond for costs is fixed in the sum of $250.

Dated, March 4th, 1936.

ALFRED C. COXE,
U. S. D. J.

Claimants' Assignment of Errors.

364

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In proceedings for reorganization of a corporation.

No. 59,886.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

365

Now come Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer (hereinafter called the "Claimants"), creditors of United Cigar Stores Company of America, the above-named Debtor, and file the following assignment of errors upon which they will rely upon prosecution of the appeal in the above-entitled proceedings from the order of the United States District Court for the Southern District of New York dated February 4, 1936,
366 and filed on or about February 5, 1936, and say that said order dated February 4, 1936, was and is erroneous in law and in fact:

1. In so far as it fails to determine that the amount of the claim of the Claimants in excess of the sum of $44,377.55, the amount of the statutory "three-year rent" claim, is provable and allowable herein in subordination to other provable claims but in priority to the interests of all stockholders of the Debtor.

2. In so far as it fails to determine the amount 367
of the claim of the Claimants in excess of said sum of $44,377.55.

3. In so far as it fails to determine that, if the amount of the claim of the Claimants in excess of said sum of $44,377.55 is not provable and allowable, it remains a charge upon the assets of the Debtor, or any corporation to which the assets of the Debtor may be transferred, in priority to the interests of all stockholders of the Debtor.

4. In so far as it determines that Section 77B 368
of the Bankruptcy Act extinguishes the portion of the claim filed by the Claimants in excess of said sum of $44,377.55, and limits their right to participate in the above-entitled proceedings to said amount, and in so far as it determines that said statute, so construed, is constitutional.

5. In so far as it fails to determine that the provision or provisions of Section 77B extinguishing the portion of the claim of the Claimants in excess of the sum of $44,377.55 and limiting their right to participate herein to said sum are unconstitutional in that they exceed the 369
power conferred upon the Congress by the Bankruptcy Clause of the Constitution of the United States (Article I, Section 8, Clause 4) and violate the Tenth Amendment of said Constitution, and in that they violate the Fifth Amendment of said Constitution by depriving the Claimants of property without due process of law and taking their property for public use without just compensation.

6. In so far as it fails to determine that, after eliminating the unconstitutional portion of the

370 statute, the claim of the Claimants is, under the statute, provable and allowable and entitled to participate in any plan of reorganization herein in full on a parity with all other provable claims.

7. In so far as it fails to determine that the claim of the Claimants herein is provable and allowable and entitled to participate in any plan of reorganization herein in full on a parity with all other provable claims.

WHEREFORE, the Claimants pray that said order, in so far as appealed from, be reversed, and that they have such other and further relief as
371 shall be just and proper.

Dated, March 3, 1936.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys and solicitors for
Caroline R. Kuehner and
Frederick G. Fischer, as
trustees under the will of
Adam Fischer,
Office and Post Office Address,
20 Exchange Place,
372 New York, N. Y.

Claimants' Citation.

By the Honorable Alfred C. Coxe, one of the United States District Court Judges for the Southern District of New York, in the Second Circuit, to Irving Trust Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor, United Cigar Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker,

Claimants' Citation.

William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation, GREETING: 373

YOU ARE HEREBY CITED and admonished to be and appear before a United States Circuit Court of Appeals for the Second Circuit, to be holden at the Borough of Manhattan, in the City of New York, in the District and Circuit above named 374 on the 3rd day of April, 1936, pursuant to a petition for appeal and an order filed in the Clerk's office of the District Court of the United States for the Southern District of New York, allowing such petition for appeal in "In the Matter of United Cigar Stores Company of America, Debtor (In proceedings for reorganization of a corporation, No. 59,886)," wherein Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, are the appellants and you are appellees, to show cause, if any there be, why the order of this Court in said petition mentioned should not be 375 corrected and why speedy justice should not be done to the parties in that behalf.

GIVEN UNDER MY HAND at the Borough of Manhattan, in the City of New York, in the District and Circuit above named, this 4th day of March, in the year of our Lord one thousand nine hundred and thirty-six, and of the Independence of the United States the one hundred and sixtieth.

ALFRED C. COXE,
United States Judge for the Southern District of New York in the Second Circuit.

Claimants' Bond.

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MASSACHUSETTS BONDING AND INSURANCE COMPANY

Home Office, Boston, Massachusetts.

DISTRICT COURT OF THE UNITED STATES OF AMERICA,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

IN THE SECOND CIRCUIT.

BOND FOR DAMAGES AND COSTS.

377 In Proceedings for Reorganization of a corporation.

No. 59,886.

The petitioners, Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, claimants herein.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

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KNOW ALL MEN BY THESE PRESENTS, That MASSACHUSETTS BONDING AND INSURANCE COMPANY, a corporation organized under the laws of the Commonwealth of Massachusetts, authorized to transact business in the State of New York, having an office and place of business at 130 William Street, Borough of Manhattan, City of New York, is held and firmly bound unto Irving Trust Company, as trustee of the estate of United Cigar

Stores Company of America, Debtor, United Cigar 379
Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation, in the sum of TWO HUNDRED FIFTY AND 00/100 ($250.00) DOLLARS, to be paid to the said Irving Trust Company, as trustee of the estate of United Cigar Stores Company of 380
America, Debtor, United Cigar Stores Company of America, Jacob Ruppert Realty Corporation, Grayson M-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation, for the payment of which, well and truly to be made, the said MASSACHUSETTS BONDING AND INSURANCE 381
COMPANY binds itself, its successors and assigns, jointly and severally, firmly by these presents.

Sealed with its seal and dated this 4th day of March, in the year of Our Lord One Thousand Nine Hundred and Thirty-six.

WHEREAS, the petitioners, Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, claimants herein, have prosecuted an appeal to the United States Circuit Court of Appeals for the Second Circuit,

382 to reverse the order dated the 4th day of February, 1936, rendered in the above entitled suit, in the District Court of the United States for the Southern District of New York,

NOW, THEREFORE, the condition of this obligation is such, that if the above named Caroline R. Kuehner and Frederick G. Fischer, as trustees under the will of Adam Fischer, claimants herein, shall prosecute and appeal to effect, and answer all damages and costs if it fail to make said appeal good, then this obligation shall be void, otherwise the same shall be and remain in full
383 force and virtue.

MASSACHUSETTS BONDING AND INSURANCE COMPANY,
By FREDERICK O. BEATTIE,
Attorney-in-Fact.

Attest:

GARRETT B. CARMAN,
Attorney-in-fact.

(Verification, etc.)

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Admission of Service of Copy of Claimants' Citation and Bond.

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DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA;

Debtor.

386 Service of a copy of the citation on appeal and of a copy of the Bond in the above entitled proceeding with notice of filing thereof is hereby admitted this 4th day of March, 1936.

ROSENBERG, GOLDMARK & COLIN,
Attorneys for Debtor.

CRAVATH, DE GERSDORFF, SWAINE & WOOD,
Attorneys for Irving Trust Company, Trustee for the Estate of United Cigar Stores Company of America.

387 SHEARMAN & STERLING,
BERLE & BERLE,
Attorneys for Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Attorneys for Debentureholders' Protective Committee.

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corp.

MILBANK, TWEED, HOPE & WEBB,
Attorneys for Phoenix Securities Corp.

Petition for Appeal of Preferred Stockholders' Protective Committee and of Debenture-holders' Protective Committee and Order Allowing Appeal.

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UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation—No. 59886.

Claim No. 5184.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

389 Debtor.

To the Honorable the Judges of the District Court of the United States for the Southern District of New York:

Grayson M-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee of United Cigar Stores Company of America, intervenors in the above entitled proceeding pursuant to an order of this Court dated and entered herein

390 September 28, 1934, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Protective Committee for the holders of Cigar Stores Realty Holdings, Inc. Twenty-year 5½% Sinking Fund Gold Debentures, Series A, intervenors in the above entitled proceeding pursuant to an order of this Court dated and entered herein October 22, 1934, believing themselves aggrieved for the reasons specified in the Assignment of Errors filed herewith, by the order of this Court made and entered herein on February 4th, 1936, in so far as said order approved and confirmed such part of the report of Honorable Irwin Kurtz, Special

Petition for Appeal of Preferred Stockholders' Protective Committee and of Debenturcholders' Protective Committee and Order Allowing Appeal.

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Master, dated October 23, 1935, as recommended that the claim of Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, be allowed as a general claim in the amount of $44,377.55, do hereby appeal from said order of February 4, 1936 to the United States Circuit Court of Appeals for the Second Circuit, and pray that their appeal may be allowed and that a citation may be granted, directed to Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, Irving Trust 392
Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor, Jacob Ruppert Realty Corporation, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee and Phoenix Securities Corporation, commanding them to appear before the United States Circuit Court of Appeals for the Second Circuit, to do and receive what may appertain to justice to be done in the premises, and that a transcript of the record upon which said order of February 4, 1936 was based, and of all proceedings relating to said claim, duly authenticated, be transmitted to the United States 393
Circuit Court of Appeals for the Second Circuit.

Dated, New York, N. Y., March 4, 1936.

GRAYSON M-P. MURPHY, G. W. BAKER, WILLIAM DE KRAFFT and BENJAMIN GRAHAM, as a Preferred Stockholders' Protective Committee of United Cigar Stores Company of America,

By: SHEARMAN & STERLING,
BERLE & BERLE,
Their Attorneys and Solicitors.

and

Petition for Appeal of Preferred Stockholders' Protective Committee and of Debentureholders' Protective Committee and Order Allowing Appeal.

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LEWIS L. STRAUSS, BURNETT WALKER and MAURICE WERTHEIM, as a Debentureholders' Protective Committee,
By: DAVIS, POLK, WARDWELL, GARDINER & REED,
Their Attorneys and Solicitors.

SHEARMAN & STERLING,
55 Wall Street,
Borough of Manhattan,
395 New York, N. Y.

and

BERLE & BERLE,
70 Pine Street,
Borough of Manhattan,
New York, N. Y.
Attorneys and Solicitors for Preferred Stockholders' Protective Committee, as aforesaid.

DAVIS, POLK, WARDWELL, GARDINER & REED,
15 Broad Street,
396 Borough of Manhattan,
New York, N. Y.
Attorneys and Solicitors for Debentureholders' Protective Committee, as aforesaid.

The foregoing appeal is hereby allowed this 4th day of March 1936, upon giving bond conditioned as required by law in the sum of $250.00.

ALFRED C. COXE,
United States District Judge for the
Southern District of New York.

Assignment of Errors of Preferred Stockholders' Protective Committee and of Debentureholders' Protective Committee.

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UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In Proceedings for Reorganization of a Corporation.

No. 59886.

Claim No. 5184.

In the Matter

of

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UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

Now comes Grayson M-P. Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee of United Cigar Stores Company of America, intervenors in the above entitled proceeding, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Protective Committee for the holders of Cigar Stores Realty Holdings, Inc., Twenty-year 5½% Sinking Fund Gold Debentures, Series A, intervenors in the above entitled proceeding, and file the following assignment of errors upon which they will rely upon prosecution of the appeal herein from the order of the United States District Court for the Southern District of New York made and entered February 4, 1936, and say that said order of February 4, 1936 is erroneous in so far as it approves and confirms such part of the report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935, as recommends that the claim of Frederick G. Fischer and Caro-

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line R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, be allowed as a general claim in the amount of $44,377.55, and in so far as said order of February 4, 1936 approves and confirms the rulings of said Special Master at the hearing on said claim, and, without limiting the generality of the foregoing, the said order of February 4, 1936 is erroneous for the following reasons:

401 1. The Court erred in approving and confirming so much of said report as refers

(a) To the purposes of the enactment of Section 77B of the Bankruptcy Act,

(b) To the alleged circumstance that a reorganization under Section 77B should include every possible claim existing against the Debtor, whether such claim be absolute, conditional, contingent or otherwise,

(c) To the alleged circumstance that there can be no distinction under Section 77B between provable and non-provable claims, as

402 existed in the ordinary bankruptcy liquidation proceeding.

as having any bearing on the legal questions presented by the claim herein or the objections made thereto.

2. The Court erred in approving and confirming so much of said report as decides that a landlord whose lease has been rejected by a Trustee and the premises returned has a claim under Section 77B for damages where the lease contains a covenant of indemnity.

3. The Court erred in approving and confirm-

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ing so much of said report as decides that the fact that such a landlord as the present claimants could not maintain an action at common law upon the indemnity covenant contained in the lease until the expiration of the term makes no difference to the aims and purposes of Section 77B and the results that were sought to be obtained therefrom, and that such a landlord has a claim under Section 77B which would necessarily have to be included in and disposed of in a reorganization proceeding.

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4. The Court erred in approving and confirming so much of said report as determines that a consideration of the purposes of Section 77B and any of the language of Section 77B requires that the landlords' claim herein be allowed to the extent of the damages that could be legally provable.

5. The Court erred in approving and confirming so much of said report as determines that the intent of Congress in the enactment of Section 77B was to grant a landlord a right to an immediate allowance in a reorganization proceeding, where there had been a rejection of his unexpired lease, irrespective as to whether his rights were based upon a covenant of damages or a covenant of indemnity with a clause for immediate assessment of damages or at the expiration of the term, and irrespective as to whether an action could be maintained immediately at common law upon any such covenant of indemnity.

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6. The Court erred in approving and confirming so much of said report as refers

(a) To the alleged intent of Congress to

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free a Debtor of all future liability on executory contracts of indemnity by proceedings in reorganization where there has been a rejection of the lease either by a Trustee or pursuant to an order of the Court,

(b) To the alleged purpose of Congress to effect a present, immediate disposition and adjustment of all claims, actual or contingent, and to fix the present value of the contract or the amount of the damage suffered as a

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result of such rejection of the unexpired lease by the Trustee in Bankruptcy or by order of the Court, so as to efficiently and expeditiously aid and carry through the purposes of reorganization,

as having any bearing on the legal questions presented by the claim herein or the objections made thereto.

7. The Court erred in approving and confirming so much of said report as determines that a claim based upon the covenant of indemnity contained in the lease upon which the claim herein

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is based can be evaluated in a Section 77B proceeding and is reasonably susceptible of immediate valuation, and that loss of rents over a period of time in the future can be presently ascertained by the difference between the rent reserved and the rental value for the balance of the term, or in any other manner.

8. The Court erred in approving and confirming so much of said report as determines that the landlords' claim herein should be allowed to the extent of three years' rent on an equal parity with other provable claims, and that such an al-

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lowance will carry out the purposes sought to be accomplished by Section 77B, and is just and proper, and is in accordance with the express provisions of Section 77B, subdivision (b).

9. The Court erred in approving and confirming so much of said report as determines that the report of the Hon. Thomas D. Thacher, acting as Special Master in the matter of Radio-Keith-Orpheum Corporation, Debtor, does not affect or is not applicable to the legal questions presented by the claim herein and the objections made thereto.

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10. The Court erred in approving and confirming so much of said report as attempts to distinguish the report of the Hon. Thomas D. Thacher, acting as Special Master in the matter of Radio-Keith-Orpheum Corporation, Debtor.

11. The Court erred in approving and confirming so much of said report as refers to the time limit within which proofs of claim must be filed in a reorganization proceeding as having any bearing on the legal questions presented by the claim herein and the objections made thereto.

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12. The Court erred in approving and confirming so much of said report as recommends that damages measured by the difference between the rent reserved and the reasonable rental value should be assessed upon the hearing held upon the objection to the claim, disposed of then, and the amount of the Debtor's obligations immediately determined, and that such a rule would accomplish the purposes and come within the scope contemplated by Section 77B and would be workable, feasible, and of general application.

13. The Court erred in approving and confirm-

412 ing so much of said report as recommends that the landlords' claim herein should be allowed in the sum of $44,377.55 as a general claim.

14. The Court erred in approving and confirming the ruling of the Special Master at the hearing on the claim in admitting evidence as to the rental value of the demised premises on or about August 29, 1932. The evidence, introduced in a supplementary stipulation of facts to which counsel reserved the right to make certain objections
413 as to its admissibility in evidence, was substantially as follows:

> That Charles N. Schragger, a real estate appraiser doing business in the City of Trenton, State of New Jersey, is a duly qualified expert on rental values of real estate in the City of Trenton, New Jersey, and particularly real estate situated in the portion of said city in which the premises covered by the lease hereinafter mentioned are situated, and that if called as an expert witness at the hearing to be held before Hon. Irwin Kurtz,
> 414 as Special Master in the above-entitled proceeding, on the objections to the claim of Caroline R. Kuehner and Frederick G. Fischer, as Trustees under the Last Will and Testament of Adam Fischer, deceased, against the above named Debtor, he would testify as follows:
>
> The fair rental value as of August 29, 1932 of the premises covered by the lease dated October 18, 1926, made by Caroline R. Kuehner and Edward A. Fischer, as Executors of and Trustees under the Last Will and Testament of Adam Fischer, deceased, and others,

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as landlords, to the Debtor, as tenant, for a term commencing on August 29, 1932, and ending on March 31, 1946, under a lease containing the same provisions as those contained in said lease dated October 18, 1926, except as to the term of the leasehold, is $4,750 a year net. The fair rental value of said premises as of August 29, 1932, for a term commencing November 14, 1932, and ending on March 31, 1946, under a lease containing the same provisions as those contained in said lease dated October 18, 1926, except as to the term of the leasehold, is the same, to wit, $4,750 a year net.

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The fair rental value as of November 14, 1932, of said premises for a term commencing on November 14, 1932, and ending on March 31, 1946, under a lease containing the same provisions as those contained in said lease dated October 18, 1926, except as to the term of the leasehold, is also $4,750 a year net.

That in his judgment there is no substantial difference in the rental values of said premises whether taken as of August 29, 1932, or November 14, 1932, as during this period there was no appreciable change in rental values.

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The aforesaid opinion as to the rental value of said premises is based not only upon the change in rental values since the lease between the landlords and the Debtor dated October 18, 1926, was made and August 29, 1932 and November 14, 1932, respectively, but also upon the factor that said premises must now be rented as an inside property separate and apart from the adjoining prem-

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ises situated on the corner of State and Broad Streets, Trenton, New Jersey, whereas both said premises and said corner premises were rented as a unit to the Debtor by the respective owners thereof on or about October 18, 1926. Said corner premises were relet as a separate unit, under a lease negotiated by said Charles N. Schragger for a term of ten years; that, accordingly, in his opinion there will be no possibility whatever

419 of reletting during said ten-year period the premises covered by the lease dated October 18, 1926, in conjunction with said corner premises.

That the present return from the premises in question is only a net amount of $3,000 a year, but that over the period of approximately fourteen (14) years said premises should return a net annual rental, as previously stated, of $4,750.

15. The court erred in holding that the claimants herein are entitled to immediate damages

420 as arbitrarily fixed by the provisions of Section 77B of the Bankruptcy Act.

16. The Court erred in failing to disaffirm the whole of said report of Hon. Irwin Kurtz, Special Master, dated October 23, 1935.

17. The Court erred in failing to determine that the claim herein should be disallowed in whole as a general claim and barred from any participation in any plan of reorganization herein on a parity with other claims allowed or allowable as general claims herein.

WHEREFORE, Grayson M.-P Murphy, G. W.

Assignment of Errors of Preferred Stockholders' Protective Committee and of Debentureholders' Protective Committee.

Baker, William de Krafft and Benjamin Graham, as a Preferred Stockholders' Protective Committee, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Debentureholders' Protective Committee, pray that said order of February 4, 1936 be reversed in part and that the aforesaid claim be determined to be disallowed in whole as a general claim and barred from any participation in any plan of reorganization herein on a parity with other claims allowed or allowable as general claims herein.

Dated, March 4, 1936.

SHEARMAN & STERLING

and

BERLE & BERLE,
Attorneys and Solicitors for
Preferred Stockholders' Protective Committee,
Office and Post Office Addresses respectively,
55 Wall Street,
70 Pine Street,
Borough of Manhattan,
New York City, N. Y.

and

DAVIS, POLK, WARDWELL,
GARDINER & REED,
Attorneys and Solicitors for
Debentureholders' Protective Committee,
Office and Post Office Address,
15 Broad Street,
Borough of Manhattan,
New York City, N. Y.

Citation on Cross-Appeal.

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By the Honorable Alfred C. Coxe, one of the United States District Court Judges for the Southern District of New York, in the Second Circuit, to Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, Irving Trust Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor, Jacob Ruppert Realty Corporation, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation,

425 GREETING:

YOU ARE HEREBY CITED and admonished to be and appear before a United States Circuit Court of Appeals for the Second Circuit, to be holden at the Borough of Manhattan, in the City of New York, in the District and Circuit above named on April 3rd, 1936, pursuant to an appeal duly obtained and filed in the Clerk's office of the District Court of the United States for the Southern District of New York, wherein Grayson M-P. Murphy, G. W. Baker, William de Krafft and
426 Benjamin Graham, as a Preferred Stockholders' Protective Committee of United Cigar Stores Company of America, intervenors, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Protective Committee for the holders of Cigar Stores Realty Holdings, Inc., Twenty Year 5½% Sinking Fund Gold Debentures, Series A, intervenors, are the appellants and you are appellees, to show cause, if any there be, why the order of this Court in said appeal mentioned should not be corrected and why speedy justice should not be done to the parties in that behalf.

GIVEN UNDER MY HAND at the Borough of Manhattan, in the City of New York, in the District and Circuit above named, this 4th day of March, in the year of our Lord, One thousand nine hundred and thirty-six, and of the Independence of the United States the One hundred and sixtieth. 427

(Sgd.) ALFRED C. COXE,
United States Judge for the Southern District of New York in the Second Circuit.

(C. W.)

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Bond for Costs on Cross-Appeal.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

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KNOW ALL MEN BY THESE PRESENTS, that the GREAT AMERICAN INDEMNITY COMPANY, a corporation organized and existing under the laws of the State of New York, with an office and place of business at No. 1 Liberty Street, New York City, New York, as Surety, is held and firmly bound unto Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, Irving Trust Company, as

Trustee of the Estate of United Cigar Stores Company of America, Debtor, Jacob Ruppert Realty Corporation, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation, in the sum of Two hundred fifty and 00/100 ($250.00), to be paid to the said Frederick G. Fischer and Caroline R. Kuehner, as Executors and Trustees under the Will of Adam Fischer, Irving Trust Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor, Jacob Ruppert Realty Corporation, Peter Grimm, Stewart C. Pratt and W. Howard Wright, as a Landlords' Protective Committee, and Phoenix Securities Corporation, for the payment of which, well and truly to be made, it binds itself, its successors and assigns, firmly by these presents.

Sealed with our seals and dated this 4th day of March, 1936.

WHEREAS, Grayson M-P Murphy, G. W. Baker, William de Krafft and Benjamin Graham, as a preferred Stockholders' Protective Committee of United Cigar Stores Company of America, intervenors, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Protective Committee for the holders of Cigar Stores Realty Holdings, Inc. Twenty-year 5½% Sinking Fund Gold Debentures, Series A. intervenors believing themselves aggrieved are about to prosecute an appeal to the United States Circuit Court of Appeals for the Second Circuit from an order of this Court made and entered herein on February 4th, 1936.

NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION IS SUCH, that if the above named Grayson M-P Murphy, G. W. Baker, William de Krafft and

Benjamin Graham, as a Preferred Stockholders' Protective Committee of United Cigar Stores Company of America, intervenors, and Lewis L. Strauss, Burnett Walker and Maurice Wertheim, as a Protective Committee for the holders of Cigar Stores Realty Holdings, Inc. Twenty-year 5½% Sinking Fund Gold Debentures, Series A. intervenors shall prosecute said appeal to effect and answer all damages and costs, if they fail to make good their plea, then this obligation shall be void; otherwise the same shall be and remain in full force and virtue. 433

GREAT AMERICAN INDEMNITY COMPANY 434

By JAMES E. SWEENEY, Attorney-in-Fact.

Bond No. B-58,821
(Seal)

[Acknowledgment and Justification.]

435

Opinion of Judge Knox.

436

The within report of the Special Master is confirmed with the exception that the claim as allowed shall represent the extent of claimant's right to participate in these proceedings. In my opinion, the provisions made by Section 77 b for the allowance of claims of landlords upon breached real estate leases were intended to put at rest the interminable speculative considerations that had to be taken into account in arriving at damages growing out of broken leases. In a proposed reorganization it is essential that claims be known and fixed at an early date—it is better that dam-
437 ages be fixed arbitrarily, as was done, than they should depend upon the attempts of parties in interest, assisted by experts, to read the future.

1/18/36

JNO. C. KNOX,
U. S. D. J.

UNITED CIGAR STORES CO.

438

Stipulation as to Record.

439

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Appellants,

440

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Appellees.

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Cross-Appellants,

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees, et al.,
Cross-Appellees.

441

IT IS HEREBY STIPULATED AND AGREED that the foregoing is a true transcript of the record of the United States District Court for the Southern District of New York in the above-entitled matter as agreed on by the parties, and that the Clerk of said Court may certify the same as correct.

Dated, New York, March 19th, 1936.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Claimants, Caroline R. Kuehner and Frederick G. Fischer, as trustees.

442 CRAVATH, DEGERSDORFF, SWAINE & WOOD,
Attorneys for Irving Trust Company, as trustee.

SHEARMAN and STERLING,

and

BERLE & BERLE,
Attorneys for Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
443 Attorneys for Debentureholders' Protective Committee.

M. CARL LEVINE,
Attorney for Jacob Ruppert Realty Corporation.

MILBANK, TWEED, HOPE & WEBB,
Attorneys for Phoenix Securities Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,
Attorneys for Landlords' Protective
444 Committee.

Clerk's Certificate.

UNITED STATES DISTRICT COURT, 445

SOUTHERN DISTRICT OF NEW YORK.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER,
as trustees,
Appellants,

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Appellees. 446

GRAYSON M-P. MURPHY, et al., as a Preferred Stockholders' Protective Committee, et al.,
Cross-Appellants,

CAROLINE R. KUEHNER and FREDERICK G. FISCHER,
as trustees, et al.,
Cross-Appellees.

I, CHARLES WEISER, Clerk of the District Court of the United States of America for the Southern District of New York, do hereby CERTIFY that the foregoing is a correct transcript of the record of the said District Court in the above-entitled matter 447 as agreed upon by the parties.

IN TESTIMONY WHEREOF, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, this 20th day of March, in the year of our Lord one thousand nine hundred and thirty-six, and of the independence of the said United States the one hundred and sixtieth.

CHARLES WEISER,
Clerk.

(Seal)

[fol. 150] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

CAROLINE R. KUHNER and FREDERICK G. FISCHER,
Appellants,

against

IRVING TRUST COMPANY, Trustee, Appellee, and Others

Before Manton, L. Hand and Augustus N. Hand, Circuit Judges

Appeals from an order of the District Court for the Southern District of New York allowing a claim of lessors for future rent in a reorganization proceeding under §77B of the Bankruptcy Act.

Rollin Browne, for the claimants.
William D. Whitney, for Irving Trust Company, Trustee.
Edgar C. Crossman, for the Debenture Holders Committee.
Sanford H. E. Freund, for the Preferred Stockholders' Committee.
M. Carl Levine, for Jacob Ruppert Realty Corp'n., Amicus Curiæ.

L. HAND, Circuit Judge:

These appeals arise from a claim by lessors against a lessee, the debtor, in a reorganization proceeding under §77B of the Bankruptcy Act. The debtor had entered the locus in quo under a lease from the claimants by which it agreed that, if it should be adjudicated a bankrupt, they might reenter and that it would then "indemnify the Land-[fol. 151] lords against all loss of rent which the Landlords may incur by reason of such termination during the residue of the term". The debtor was adjudicated in 1932, before §77B was passed, and its trustee rejected the lease, after which the lessors reentered. They have filed a claim for the difference between the rent reserved and the present value of the term; the judge allowed the claim, but limited it to three years rent, in accordance with subdivision (b) (10) of §77B. A committee of debenture holders and a committee of preferred shareholders appeal, asserting that it should be

expunged in toto; the lessors appeal because it has been limited as against shareholders; they concede that it should be subordinate to the claims of other creditors so far as it exceeds the limit.

The first question is as to the appeals of the two committees which go to the allowability of any part of the claim. The argument is that only the breach of the covenant to indemnify the lessors is provable, and that as to this, since the period of the term must expire before they can know what their loss is, or, indeed whether they have suffered any, the damages must await the expiration of the period of the term; and that it cannot be liquidated now. Subdivision (b) (10) certainly makes the "rejection" of the lease a factor in recovery, though it does not say on what else the recovery shall be based, except that it shall be for the lessor's "injury". When first introduced into the House, (H. R. 5884), the section did not expressly mention leases; the language merely was that any rejection of an executory contract should be a breach, and should result in a claim for damages [fol. 152] unless the contract was ended by "reentry", among other things.* However, that word showed that leases were included; and if the act had followed the original House bill the committees would certainly be right in saying that the claim at bar could stand only on the covenant, if it could on that. It is very difficult to know what the section really means, as it finally did emerge. For instance, "rejection" by the lessee under the judge's direction is classed with "rejection" by a receiver or trustee, as though its legal effect were the same. Obviously it is not; rejection by a receiver or trustee merely ends the possibility that he may become an assignee of the term by operation of law; it does not create the lessee's default, though of course acceptance would relieve him in futuro. But, whatever was meant, we cannot suppose that Congress was trying to make over the contract by imposing a liability for

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*"In case any executory contract shall be rejected, the same shall be deemed to have been breached and the holder shall be entitled to file a claim for damages for such breach and such claim may be allowed provided such contract shall not have been terminated by forfeiture, reentry or otherwise."

future rent on the lessee after the term had ended. Indeed, we should have considerable doubt whether the bankruptcy power would support such an effort. At least the original bill attempted nothing of the sort, and a change of language so inartificial and obscure ought not, it seems to us, be given so extravagant an effect. It is not necessary to read it so; it is enough if the language be taken to mean that the "rejection" of a lease shall be a present breach of all the [fol. 153] lessee's promises, either to pay rent, to rebuild, to cover taxes or whatever else they may be. Indeed, if it continues his liability after reentry, it was redundant to include covenants "for damages or indemnity". We do not therefore believe that this language creates new claims after reentsy, and the committees, so far, are right. We have in substance already so declared, and we adhere to what we said. In Re United Cigar Stores Co., Ex parte Otis Land Estate Co., 83 Fed. (2) 202, 206.

But in the result the committees are wrong. At petition filed the lessee was under an absolute liability to indemnify the lessors, though in an unknown amount; and indeed it was not even certain that there would be any recovery at all. That the payment was to be made in the future was not indeed material, but the ad damnum was so uncertain that before the reorganization act the claim could not have been proved. Manhattan Properties v. Irving Trust Co.; 291 U. S. 320. The question is how far that act has changed the law. Again the language is obscure, but now the purpose is apparent; it was at least to give lessors some immediate relief which had been impossible in bankruptcy. This is obvious in §63 (a) (7), and the language there is like that of §77B (b) (10). A present and definite claim "for damages and indemnity" was to be provable, and its amount could be computed only in case a present appraisal of the future value of the term was accepted as one factor in the equation. Otherwise the statute accomplished nothing. We hold therefore that the claim is to be liquidated like a claim for breach of an executory contract for chattels; that is, by discounting the future payments and subtracting the appraised value of the term from their sum.

[fol. 154] There remains the question of limitation; first whether the statute meant to limit such claims except as against other creditors; second, whether it was constitutional, if it did. As we have already shown, the House bill

ranked such claims generally on a parity with other debts. The Senate at first let this stand as to lessors in reorganizations, but limited it in bankruptcy to one year. Later it changed its position as to reorganizations by subordinating the claim to other debts so far as it exceeded one year's rent. In conference the present form was adopted; the words, "ranking on a parity" etc., then becoming unnecessary, strictly speaking. The construction suggested by the lessors might indeed have been a compromise between the position of the two houses, but if it was, it is impossible to imagine why it should have been put in the words chosen. The Senate had just shown that it knew how to say that the lessor should have an unlimited subordinate claim; the substitute expressly declared that the claim should in general be on a parity, but that it should be limited. How this can be wrenched into saying that in addition it should be allowed against shareholders without limit we cannot understand; it is more reasonable to assume that the clause was merely vestigial. We have no doubt that such claims are provable only so far as they share in "parity".

The supposed unconstitutionality of the act, so read, depends upon the fact that lessors' claims, though calculated in customary ways, are not only denied equal standing with other debts, which would indeed be permissible, but are not [fol. 155] allowed against shareholders. This was bad enough, the argument runs, when the debt was not discharged, but now even that remedy is taken away, and in its stead an inadequate and truncated substitute is provided. This position presupposes that the appraisal of the future value of real estate is so reliable a basis for the distribution of a fund in court, that Congress was obliged to treat it as good against shareholders. No doubt the present tendency is to accept more speculative evidence of damages than formerly, rather than turn away a promisee empty-handed; but there are still limits, and indeed there always must be, if human affairs are not to be subject to the fancies of any dreamer who has the hardihood to take an oath. The appraisal of realty at a distant time is the merest guess; nobody can possibly know anything about it, and one man's guess is nearly as good as another's. For this reason Congress might circumscribe its use to the near future, not only as against creditors, but against the lessee itself. That would be no more drastic or unfair than

the common-law had been again and again. The lessors reply that this might be well enough, if Congress had really acted on that theory, but it did not. Such a principle would require the limit to be reckoned in future losses, not in rents; as for example, by saying that the difference between the rents and the appraised future value should be allowed for only five years. Three years' gross rents has no relation whatever to three or five years' losses. For example, the term might have a value equal to three-quarters of the rents; if it did, the lessor could prove twelve years' losses; [fol. 156] and a present forecast over that whole period would be treated as reliable evidence. If on the other hand the value of the term was only one-fourth of the rents, the lessor could recover only four years' losses; and any further forecast would be considered too conjectural. The limit actually fixed cannot therefore be defended on the supposed principle; and the statute is mere caprice.

The mere fact that the test is a rude one will not, however, invalidate the act if it has some rational relation to the end to be achieved; courts do not sit to enforce counsels of perfection upon legislatures. Lindsley v. Natural Carbonic Gas Co., 220 U. S. 61, 78; Second Employers' Liability Cases, 223 U. S. 1, 52-53; Chicago Dock Co. v. Fraley, 228 U. S. 680, 687. The limit chosen has such a rational relation. It is indeed true theoretically that there may be cases where a lessor's losses would be recoverable for only three years, the value of the term having fallen to nothing; but those would be extreme cases and rare; ordinarily the term will have a substantial residual value and the lessor's losses will be recoverable for four or five years at least. That is a period which Congress might well fix as the maximum forecast which it would be safe to act on. There will, however, be many cases where recoverable losses will go far beyond that period, and that makes the discrimination. Primarily it is the lessee who should complain of that; he may well argue that if appraisals of the future become too conjectural at four or five years they ought not to be allowed for ten, fifteen or twenty. There are two answers to this; first, it is an objection good only in the lessee's mouth, and second, it is not good in his. It is abundantly settled [fol. 157] that to challenge a statute one must suffer a personal grievance; vicarious complaints will not serve. Plymouth Coal Co. v. Pennsylvania, 232 U. S. 531, 544, 545;

Jeffery Mfg. Co. v. Blagg, 235 U. S. 571, 576; Arizona Employers Liability Cases, 250 U. S. 400, 429; Oliver Iron Co. v. Lord, 262 U. S. 172, 180-181; Gorieb v. Fox, 274 U. S. 603, 606. Moreover, a lessee could not complain*t*; he is getting a discharge upon a payment which he cannot show is too great until the occasion is past. Therefore, the lessor's only grievance comes to this, that when his losses are large he is not treated equally with those whose losses are small. If, as we think, no lessor is unjustly treated as against his lessee, this is a complaint to which we are not disposed to lend an auspicious ear. No doubt inequality without basis is favoritism, and favoritism arouses resentment among just persons, even when the unpreferred would have no complaint, if they stood alone. But all inequalities are not of equal moment and here there is an attempt at equality by giving all members of the class a share in the pot, measured by a uniform rule. The Fifth and Fourteenth Amendments are not manuals or vade mecums; they stand rather for attitudes of the will then for commands to conduct. Certainly in cases like this where the law is not an effort to compose conflicting group interests,—though possibly in those cases too,—perhaps the best way to apply their precepts is to ask whether they shock one's native and unsophisticated sense of fair play. Nor is that irrational either, for a legislature is justified in embodying that sense into law; it is not obliged to, and usually it cannot, adjust all interests with ideal nicety; nor is it bound to the best [fol. 158] contrivances, as we have just said. Nobody should be shocked that in a class of claims like these, so inherently uncertain, a piepowder standard is chosen, even though it operates unevenly, as unquestionably it does.

There remains only the fact that the debtor is discharged. A petition under § 77B, whether voluntary or involuntary, must allege that the debtor is insolvent, or that it cannot pay its debts as they mature. Shareholders are entitled to protection as of right only "for the realization by them of the value of their equity, if any", (subd. (b) (4), § 77B). If they get an interest in the reorganized insolvent, it must be because it is desirable to continue the business under the old management, or because they will be induced to subscribe new money, or for some other reason of the sort. If, therefore, a corporation is insolvent and there is no equity, the right to pursue the lessee is a

phantom which Congress did right to ignore. It is true that corporations which cannot pay their maturing debts may have a real equity, and a discharge against them may be a substantial detriment to the creditor. But before holding that the substitute was here inadequate we must look at the position in which these lessors would have found themselves if there had been no reörganization. The corporation being in default would by hypothesis be open to dismemberment by its creditors; in that scramble the lessors would not share, for they would have no present claim. Only as their rents fell due, could they collect; unless indeed the covenant must be read as that in Hermitage Co. v. Levine, 248 N. Y. 333, in which event they would have had to wait till the end of the whole period. Such remedies [fol. 159] against a debtor are no better than if it were out and out insolvent. This reasoning does not apply when there is a fixed sum unconditionally due before petition, and possibly the limit does not then apply either. We assume that it does apply, when the lease has a covenant allowing the lessor to charge the lessee after reëntry in a single sum with the difference between the accelerated rents and the present value of the term, and he reënters after petition filed. In that situation our reasoning just above does not perhaps carry as persuasively, and we may leave the question open whether the limit is then valid. As to this lease it certainly is, and that is true whether we construe the covenant as requiring successive indemnities, or a single one at the end of the whole period.

Order affirmed.

[fol. 160] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In re United Cigar Stores Co. Kuehner v. Irving Trust. Opinion. L. Hand, C. J.

[fol. 161] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a stated term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Court House in the City of New York, on the 20th day of July, one thousand nine hundred and thirty-six.

Present: Hon. Martin T. Manton, Hon. Learned Hand, Hon. Augustus N. Hand, Circuit Judges.

In the Matter of UNITED CIGAR STORES COMPANY OF AMERICA, Debtor,

CAROLINE R. KUEHNER and Another; CARYSOM M-P MURPHY et al., Appellants

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed with costs.

It is further ordered that a mandate issue to the said District Court in accordance with this decree.

Wm. Parkin, Clerk.

[fol. 162] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In re United Cigar Stores Company of America. Order for mandate. United States Circuit Court of Appeals, Second Circuit. Filed July 20, 1936. William Parkin, Clerk.

[fol. 163] UNITED STATES OF AMERICA,
Southern District of New York:

I, William Parkin, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 162, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of In the Matter of United Cigar Stores Company of America, Debtor, Caroline R. Kuehner and another; Carysom M-P Murphy et al., Appellants, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 31st day of July, in the year of our Lord one thousand nine hundred and thirty-six, and of the Independence of the said United States the one hundred and sixty-first.

Wm. Parkin, Clerk. (Seal United States Circuit Court of Appeals, Second Circuit.)

[fol. 164] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 26, 1936

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(8426-C)

FILED
NOV 9 19
CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

Nos. 354, 151 and 260

IN THE MATTER OF

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,

Petitioners in No. 354,

MRS. JOHN S. MEADOWS,

Petitioner in No. 151,

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee,

Petitioner in No. 260,

against

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,

Respondents.

Motion to Advance by Irving Trust Company, as Trustee

and

Consent by Petitioners to Granting of Said Motion and Waiver of Notice Thereof

---

New York, November 4, 1936.

WILLIAM D. WHITNEY,
Counsel for Respondent,
Irving Trust Company, as Trustee.

DONALD C. SWATLAND,
R. L. GILPATRIC,
Of Counsel.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

Nos. 354, 151 and 260

IN THE MATTER

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Petitioners in No. 354,

MRS. JOHN S. MEADOWS,
Petitioner in No. 151,

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee,
Petitioner in No. 260,

against

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,
Respondents.

MOTION TO ADVANCE

To the Honorable the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Comes now Irving Trust Company, as Trustee, respondent in Nos. 354, 151 and 260, and respectfully

moves the Court to advance the above-entitled causes for hearing on an early day convenient to the Court. On October 26, 1936, this Court granted the petitions for writ of certiorari in such causes and set them down for argument in the order indicated.

All three cases involve questions as to the status of landlords' claims in proceedings under Section 77B of the Bankruptcy Act. Among such questions are the following:

1. Should the statutory provision [Section 77B (b) 10] be construed to limit landlords' claims, for loss of future rent, not theretofore provable in bankruptcy at all, to a maximum of three years' rent (plus accruals) as against the interest of the debtor's stockholders, and if so construed is the provision constitutional? (No. 354.)

2. Does the statutory provision make provable the claim of a landlord who had terminated her lease (which contained no covenant of surviving liability) after its rejection in the prior bankruptcy proceedings of the debtor (No. 260), or the claim of a landlord who accepted a surrender of her lease by assignment and released the debtor from further liability (No. 151), where such termination, surrender and release took place before the enactment of the statute?

3. Does the rejection of a lease, during the prior bankruptcy proceedings of the debtor and prior to the enactment of the statute, constitute the basis of a claim under the statute, notwithstanding

that at the time of institution of the subsequent reorganization proceedings the landlord no longer has a claim enforceable under the substantive law of landlord and tenant (Nos. 151 and 260)?

United Cigar Stores Company of America was adjudicated bankrupt on August 29, 1932 and on June 9, 1934 its petition for reorganization under Section 77B of the Bankruptcy Act was approved. The time for filing claims in such reorganization proceedings as fixed by the District Court expired on October 10, 1934.

Claims and interests of creditors and stockholders of the debtor have been allowed by the courts below in approximately the following amounts:

General creditors, exclusive of Landlord claimants	$4,700,000
Landlord claimants	$3,500,000
Preferred stockholders	171,357 shares
Common stockholders	5,370,660 shares

The respondent Reorganization Committee, consisting of representatives of a substantial proportion of such creditors and claimants and the preferred stockholders, has been engaged in the formulation of a plan of reorganization, and the Trustee is advised that such Committee (subject to the receipt of a report now under preparation by a firm of engineering experts) has carried the draft of plan to an advanced stage of preparation. The grant by this Court of writs of certiorari in the above-mentioned cases has, however, caused uncertainty as to the disposition of landlords' claims totaling approximately $7,000,000 (using the three-

year rent basis provided in Section 77B (b) as a maximum).*

In the opinion of the respondent Trustee, therefore, no plan of reorganization of the Debtor can be consummated until the cases pending before this Court have been determined, and reversal by this Court of the decisions in certain of the above-entitled cases would undoubtedly require changes in any presently prepared plan of reorganization.

This estate, one of the largest being administered by the Federal courts under the provisions of Section 77B, has been pending in administration for more than four years. It is naturally the desire of all parties to return the management of the debtor as promptly as possible to private hands and to effect a distribution to the creditors and stockholders of their interests in the estate of the debtor as promptly as possible. Past delays in reorganization have been unavoidable due to the vast amount of litigation involved, and important causes have been advanced from time to time by the courts below. It is earnestly desired that all future time to be consumed in litigation be shortened in so far as consistent with the convenience of this Court and the requirements of justice with respect to the claims of the creditors involved in these cases.

WHEREFORE, respondent prays that Nos. 354, 151 and 260 be set down for hearing on an early day convenient to this Court, not earlier than December 7, 1936, and that full

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*But even the validity of the three-year rent provision is called in question in No. 354.

time be allowed for the argument of each of said causes which will be presented separately.

WILLIAM D. WHITNEY,
Counsel for Respondent,
Irving Trust Company, as Trustee of the Estate of United Cigar Stores Company of America, Debtor,
Office and P. O. Address:
No. 15 Broad Street,
Borough of Manhattan,
New York, N. Y.

DONALD C. SWATLAND,
R. L. GILPATRIC,
Of Counsel.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936

Nos. 354, 151 and 260

IN THE MATTER

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Petitioners in No. 354,

MRS. JOHN S. MEADOWS,
Petitioner in No. 151,

CITY BANK FARMERS TRUST COMPANY, Assignee of Florence H. Bugbee,
Petitioner in No. 260,

against

IRVING TRUST COMPANY, as Trustee of the Estate of the above-named Debtor, *et al.*,
Respondents.

CONSENT TO MOTION TO ADVANCE AND WAIVER OF NOTICE

The undersigned hereby waive notice of the foregoing motion and consent to the granting thereof on condition that said causes shall not be argued as one cause but that

full time shall be allowed for the argument of each of said causes..

Dated, New York, N. Y., November 4, 1936.

ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
HENRY L. GLENN,
Counsel for petitioners Caroline R. Kuehner and Frederick G. Fischer, in cause No. 354.

ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for petitioner City Bank Farmers Trust Company, Assignee of Florence H. Bugbee, in cause No. 260.

PERLIE P. FALLON,
Counsel for petitioner Mrs. John S. Meadows, in cause No. 151.

M. CARL LEVINE,
Counsel for respondent Jacob Ruppert Realty Corporation.

MITCHELL, TAYLOR, CAPRON & MARSH,

and

RALPH MONTGOMERY ARKUSH,
Counsel for respondent Landlords' Protective Committee.

SHEARMAN & STERLING,

and

BERLE & BERLE,
Counsel for respondent Preferred Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Counsel for respondent Debentureholders' Protective Committee.

MILBANK, TWEED, HOPE & WEBB,
Counsel for respondent Phoenix Securities Corporation.

WRIGHT, GORDON, ZACHRY & PARLIN,
Counsel for respondent Reorganization Committee.

FILE COPY

SEP 10 1936

CHARLES ELMORE CRO
CLER

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 354

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Petitioners,

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders Protective Committee, *et al.*,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT OF PETITION.

ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
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THE COURT PRESS, N. Y. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. .

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER,
as trustees,
Petitioners,

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders Protective Committee, *et al.*,
Respondents.

PETITION FOR WRIT OF CERTIORARI

To the Honorables, the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

The petitioners respectfully submit their petition for a writ of certiorari to review the decision of the United States Circuit Court of Appeals for the Second Circuit in the above case.

SUMMARY STATEMENT OF MATTER INVOLVED

This case involves the interpretation and constitutionality of the limitation on landlords' claims under Section 77B of the Bankruptcy Act (*infra*, p. 11).

The petitioners are creditors of United Cigar Stores Company of America, the debtor in corporate reorganization proceedings under Section 77B. Their claim arises out of a lease of real estate which had been rejected by the debtor's trustee in bankruptcy proceedings antedating the 77B proceedings. Under the lease covenant the petitioners are entitled to indemnity from the debtor against all loss of rent during the period of fourteen years between the termination of the lease by reentry in 1932 and the expiration of the stipulated term in 1946. Under the law of its state of incorporation in case of a winding up of the debtor, the claim of the petitioners would be recognized to its full extent in priority to any interest of stockholders. There has been no determination that the debtor is insolvent. Nevertheless, the Court of Appeals has decided that—irrespective of how large may be the participation accorded to stockholders—the petitioners' right to participate in the reorganization is limited to the arbitrary amount specified in clause (10) subdivision (b) of Section 77B (referred to herein as "three years rent"). Such amount is concededly less than the difference between the future rent payments, discounted, and the appraised value of the remaining term. The court below refused to allow the balance of such difference over three years rent in subordination to debts provable under Section 63(a) of the Act (herein referred to as "provable debts"), or to interpret the statute as requiring the preservation of the petitioners' rights in priority to stockholders to the extent they may turn out to exceed three years rent.

FACTS

The petitioners' predecessors leased to the debtor premises in New Jersey for a term commencing in 1926 and expiring in 1946, at a net annual rental of $10,500 for the first ten years and $11,500 thereafter (R. 46). On August 29, 1932, the debtor filed its voluntary petition in bankruptcy, was adjudicated and abandoned the premises. On November 14, 1932, the trustee in bankruptcy rejected the lease and abandoned the premises and on the following day the landlords re-entered (R. 6, 40), thus terminating the lease (R. 57). The lease obliged the debtor in such event to indemnify the landlords against all loss of rent which the landlords might incur by reason of such termination during the residue of the term (R. 57).

The debtor's petition for reorganization under Section 77B was filed in the bankruptcy proceedings on June 9 and approved on June 14, 1934. The petitioners filed a proof of claim (R. 4) praying that their claim "based upon or arising out of the lease * * * or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy * * * or for damages or indemnity under a covenant or covenants contained in said lease", measured by the difference between the rent reserved and the rental value for the remainder of the term, be allowed on a parity with provable debts to the extent of three years rent and that the balance be allowed in subordination to provable debts but in priority to the claims or interests of the stockholders of the debtor.

The reorganization trustee objected, asking that the claim be reduced to an amount "limited as provided by the statute" (R. 15).

At the hearing, committees representing preferred stockholders and debentureholders of the debtor objected to the allowance of the claim in any amount

(R. 21) on the ground that the petitioners could not sue on the covenant of indemnity until the expiration of the term. Thereupon the petitioners amended the proof of claim so as to pray that, to the extent that any part of the claim should be held not provable, a charge be reserved against the debtor's assets, at least in priority to any interest accorded to stockholders (R. 25).

The fair rental value of the premises for the balance of the term is $111,545.36 (R. 73). The expert testimony establishing this value was not controverted. The future installments of rent under the lease for the remainder of the term aggregate $199,237.66.

RULINGS BELOW

The Special Master recommended (1) that the claim should be allowed on a parity with provable debts to the extent of three years rent, to wit, $44,377.55 and (2) that all questions as to the balance of the claim should be reserved until the time of the classification of creditors and stockholders and the consideration of a reorganization plan (R. 93).

The District Court confirmed the Special Master's report with the exception that the extent of the petitioners' right to participate in the proceedings was limited to the amount of $44,377.55 (R. 116, 146).

On cross appeals, the Court of Appeals affirmed, holding (R. 150): (1) that the claim should be liquidated "by discounting the future payments and subtracting the appraised value of the term from their sum" (R. 152);* (2) that the claim as so

* All questions as to discount were reserved for future determination of the District Court. However, the instant claim would exceed three years rent, even if discounted on any reasonable basis.

liquidated was presently allowable up to the amount of three years rent; (3) that the limitation provision of the statute was intended to limit the petitioners' participation, as against stockholders as well as creditors, whether by way of allowance of a claim or reservation of rights; and (4) that the limitation provision, as so interpreted, was constitutional, because of supposed difficulties in liquidating the claim and because the pre-existing rights of the petitioners, of which they were deprived by the statute, were considered to be of no practical value.

QUESTIONS PRESENTED

1. Should the limitation provision be interpreted as limiting only the amount in which the petitioners' claim is allowable on a parity with provable debts, permitting the balance of the claim to be allowed in priority to the interest of stockholders?

2. If the balance of the claim is not presently allowable, does the statute preserve the residual rights of the petitioners in priority to the interest of stockholders?

3. If the statute is interpreted as limiting the petitioners' rights to a claim for three years rent, even although stockholders participate in the reorganization, is the statute to that extent unconstitutional as beyond the power of Congress under the bankruptcy clause and in contravention of the Fifth and Tenth Amendments?

The question of the constitutionality of the limitation provision was raised below (R. 28, 96-7, 123).

REASONS RELIED ON FOR ALLOWANCE OF WRIT

1. It is of public importance that doubts as to the meaning and constitutionality of the limitation provision be settled. Questions arising under other portions of Section 77B have been considered of sufficient public importance to justify review by this Court on certiorari.*

Landlords' claims constitute a large part of the claims pending against corporate debtors now in process of reorganization under Section 77B. In the present proceedings the amount of landlords' claims filed far exceeds the total amount of all other claims, and many of such claims, involving amounts in excess of three years rent, are awaiting the outcome of this case, in which the petitioners are represented by counsel for the Landlords' Protective Committee. Landlords' claims are especially frequent in cases of chain store corporations many of which, as has been publicly noted,** resorted during the recent depression to bankruptcy proceedings primarily for the purpose of escaping the burden of long term leases, and 77B proceedings have been instituted in many such bankruptcy proceedings.***

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* *Meyer* v. *Kenmore Granville Hotel Co.*, 296 U. S. 565; 297 *id.* 160; *Tuttle* v. *Harris*, 296 U. S. 567; 297 *id.* 225; *Callaghan* v. *Reconstruction Finance Corp.*, *Stitt* v. *Same*, 296 U. S. 570; 297 *id.* 464; *Duparquet Huot & Moneuse Co.* v. *Evans*, 296 U. S. 569, 297 *id.* 216; *Foust* v. *Munson S. S. Lines*, 80 L. Ed. 746; *Tennessee Publishing Co.* v. *Am. National Bank*, 80 L. Ed. 957.

** 42 Yale L. J. 1003; 33 Col. L. Rev. 231-4; 7 Univ. of Cinn. L. Rev. 164-5; see also the remarks of Representative Celler on the floor of the House (76 Cong. Rec., Pt. 2, p. 1360), with regard to the debtor in the case at bar.

*** The extent to which reorganization proceedings have been resorted to by chain store corporations is indicated by the following partial list of such corporations which are now in reorganization under Section 77B in the Southern District of New York alone: Schulte Retail Stores Corporation; D. A. Schulte

The difficulty of the questions presented is shown by the inconsistent interpretations of the statute advanced below by the various objectants. The trustee has contended that Congress intended to give the petitioners an allowable claim not in excess of three years rent in full satisfaction of their contract rights. The Debentureholders' Protective Committee has urged that Congress intended the petitioners to be held to the terms of their contract which entitled them to indemnity only at the expiration of the term of their lease. The Preferred Stockholders' Protective Committee has urged that the petitioners have no presently allowable claim, but that, nevertheless, Congress has limited their right to seek indemnity at the end of the term.

2. The questions presented are novel. So far as is known, the limitation provision is the first attempt of any legislature under any system of jurisprudence to limit the claims of a single class of creditors of an embarrassed debtor by an arbitrary formula bearing no relation to the creditor's real injury and of no utility in liquidating his claim. And when, as here, such provision is held to extinguish part of the creditors' rights for the benefit of the debtor's stock-

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Inc. of New York; D. A. Schulte, Inc. of Delaware; Huylers, Inc. of Delaware; Huyler's, New York; Schulco, Inc.; H. L. Green Co.; Bellcamp Stores, Inc.; Diamond Brothers Apparel Corp.; Steuben Taverns; Liberty Baking Corp.; Sunnydale Food Stores, Inc.; Highland Dairy Co.; Albrecht's Stores, Inc.

Some of such corporations which are in reorganization under Section 77B in other districts are as follows: Burg Company (Minn.); H. Winer Co. (Boston); Pollyanna Stores, Inc. (Conn.); Grant Lunch Corp. (Newark, N. J.); Donahoe's Inc. (Pittsburgh, Pa.); Gross Stores, Inc. (Phila., Pa.).

In recently pending reorganization proceedings of two large corporations similar questions regarding landlords' claims were also presented, but such claims were disposed of by compromise: Paramount Publix Corp. (S. D. N. Y.) and J. G. McCrory Co. (S. D. N. Y.).

holders, such legislation introduces an anomaly into the established Anglo-American law of debtor and creditor.

There is no analogy in prior bankruptcy legislation or in other provisions of the Bankruptcy Act now in force. The remark of this Court in *Louisville &c. Bank* v. *Radford,* 295 U. S. 555, 582, that no bankruptcy act had ever before undertaken to supply the bankrupt capital with which to engage in business in the future is applicable to Section 77B which, as construed below, transfers to the stockholders of the debtor an interest of substantial value belonging to the landlord creditors.

The former exclusion of landlords' claims of certain types from provability in bankruptcy in any amount furnishes no precedent. Claims not provable were not dischargeable, nor could the stockholders of the bankrupt corporation enrich themselves at the expense of the holders of non-provable claims by going through the formality of a bankruptcy sale and vesting the assets in a new company (see Landlords' Claims in Reorganization, 42 Yale L. J. 1003, 1015-1026).

Nor are the questions here discussed raised by the existing provisions for the relief of individual debtors (Section 74), railroad corporations (Section 77) and municipal corporations (Section 80). In none of those sections is there an attempt to limit landlords' claims.

The statute as interpreted below overturns established legal principles under which the rights of creditors, however contingent their claims may be, have hitherto enjoyed full protection in priority to stockholders (*Pierce* v. *United States,* 255 U. S. 398;

Northern Pacific Ry. Co. v. *Boyd,* 228 U. S. 482; *Block* v. *Bell Furniture Co.,* 111 N. J. Eq. 551).

3. The decision below departs from the principles established by the decisions of this Court in various respects, as shown in the annexed brief.

For the above reasons, the petitioners respectfully pray that a writ of certiorari issue to review the decision below.

Dated, September 4, 1936.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as Trustees,

By ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
HENRY L. GLENN,
Counsel for Petitioners.

BRIEF IN SUPPORT OF PETITION

OPINIONS BELOW

The opinion of the District Court (per Knox, *D. J.*) appears at page 146 of the record and is not officially reported. The opinion of the Court of Appeals (per L. Hand, *C. J.*) appears at page 150 of the record and is not yet officially reported.

JURISDICTION

Jurisdiction to issue the writ is vested in this Court by Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The order for mandate was entered on July 20, 1936.

STATEMENT OF THE CASE

The facts, rulings of the courts below and questions presented are set forth in the foregoing petition.

STATUTE INVOLVED

Section 77B of the Bankruptcy Act (48 Stat. 911) provides:

> "Sec. 77B. Corporate Reorganizations * * *.
>
> (b) * * * (10) * * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts * * * or other interest of whatever character. * * *

In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry. * * *

(h) Upon final confirmation of the plan, * * * the property dealt with by the plan * * * shall be free and clear of all claims of the debtor, its stockholders and creditors, except such as may consistently with the provisions of the plan be reserved * * *. Upon the termination of the proceedings a final decree shall be entered * * *. Such final decree shall discharge the debtor from its debts and liabilities, and shall terminate and end all rights and interests of its stockholders, except as provided in the plan or as may be reserved as aforesaid. * * *"

(Act approved June 7, 1934, 48 St. 911, Ch. 424, §1; U. S. C. Tit. 11, §207.)

SPECIFICATION OF ERRORS

The Court of Appeals erred in holding:

(1) that the limitation provision prohibited the allowance of the balance of petitioners' claim over three years rent in subordination to provable debts but in priority to the interest of stockholders;

(2) that the limitation provision prohibited the preservation of the petitioners' residual rights in priority to the interest of stockholders;

(3) that the limitation provision as so interpreted was a valid exercise of the bankruptcy power and did not violate the Fifth Amendment;

(4) that the petitioners had no standing to complain that other landlord creditors similarly situated would receive more favorable treatment than the petitioners as a result of the operation of the limitation provision as so interpreted.

SUMMARY OF ARGUMENT

Before the enactment of Section 77B the debtor had become obligated to the petitioners on the covenant of indemnity. The petitioners were, therefore, creditors, entitled to priority over the debtor's stockholders, and their contract rights constituted property within the protection of the constitutional guarantees. Moreover, the lease had been rejected by the trustee in bankruptcy.

Congress contemplated that in such a situation the petitioners' claim should be presently ascertained by some judicial method and allowed on a parity with provable debts up to an amount not in excess of three years rent, and that the balance, if any, of their

claim should be allowed in subordination to provable debts, but in priority to the interest of stockholders.

If the statute does not contemplate the subordinate allowance of such balance of the claim, then it requires that the debtor's liability under the covenant of indemnity, to the extent that it turns out to exceed the amount in which the claim is presently allowed, must be reserved, either in the plan or by order of the court, in priority to any interest accorded to the debtor's stockholders on the reorganization.

If the statute is construed as entirely freeing the debtor and its assets from liability to the petitioners in excess of three years rent, for the benefit of the debtor's stockholders, the statute is to that extent unconstitutional, as not falling within the bankruptcy power and as violating the Fifth and Tenth Amendments.

POINT I.

The balance of the petitioners' claim over three years rent is allowable in subordination to provable debts, but in priority to the interest of stockholders.

Even though before the enactment of Section 77B the petitioners' rights were contingent and unliquidated, the petitioners were creditors. Their right to priority over stockholders could not be displaced by discharge in bankruptcy; or by voluntary liquidation (*Pierce* v. *United States,* 255 U. S. 398); or by insolvency or winding up proceedings under the law of the state of incorporation (*Block* v. *Bell Furniture Company,* 111 N. J. Eq. 551); or by any form of reorganization (*Northern Pacific Railway Company* v. *Boyd,* 228 U. S. 482; *Howard* v. *Maxwell Motor Co., Inc.*, 269 Fed. 292, aff'd 275 Fed. 53; see Landlords'

Claims in Reorganization, 42 Yale L. J. 1003, 1015-1026).*

No statute theretofore enacted "for the relief of debtors" or for any other purpose had attempted to upset the established principle under which even contingent creditors are protected as against stockholders (*Kalkhoff* v. *Nelson,* 60 Minn. 284; *In re Mechanics Trust Co.,* 119 N. J. Eq. 141; *Block* v. *Bell Furniture Co., supra*; see also Sec. 425, N. Y. Insurance Law). The language, legislative history and underlying purpose of Section 77B indicate that Congress had no intention of attempting to upset these established rules.

A. *The language and legislative history.*

The general structure of the Act supports the interpretation that the limitation provision limits only the part of the claim allowable on a parity with provable debts. Subdivision (b) defines "creditors" as including "all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act" and defines "claims" as including "debts * * * or other interest of whatever character". The statute then specifically provides that any person injured by the rejection of an unexpired lease in the reorganization proceedings or in prior proceedings shall "for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor." These provisions clearly establish the landlord's status as a creditor to the full extent of his injury, damages or right to indemnity, and that

* *Block* v. *Bell Furniture Co.* and *Howard* v. *Maxwell Motor Co.* involved landlords' claims for loss of future rent.

status should be restricted only if and to the extent required by other equally clear and unambiguous language. There is no language anywhere in the statute which, in express terms, limits the landlord's status as a creditor. The succeeding sentence containing the limitation provision was not required in order to make the landlord a creditor or to entitle his claim to recognition, but only to fix the relative rank of his claim as compared with other claims.* Therefore, it should not be interpreted as restricting his general status as a creditor. Indeed, the fact that the limitation provision requires that the landlord's claim be treated on a parity with provable debts, subject to limitation in amount, indicates the intention of Congress that the balance of the claim, if any, be accorded subordinate treatment, since nowhere else in the statute is rank or priority prescribed (except the priority of certain unsecured claims over mortgages). If landlords' claims are limited for all purposes, the provision for parity is useless verbiage, as the Court of Appeals admits (R. 153).

The legislative history also supports the interpretation here urged. The bill, as originally passed by the House, allowed landlords' claims in full (H. R. 5884, June 2, 1933, p. 10). As passed by the Senate the bill provided that a landlord's claim should "not be treated as a claim ranking on a parity" with provable debts "except up to an amount equal to" one years rent, but that the balance, if any, of the claim should "be subordinated in rank to debts so provable" (H. R. 5884, May 7, 1934, p. 11). The only point of difference was the amount allowable on a parity,

* The language of the limitation provision originally adopted by the Senate (quoted above in the last paragraph of this page) bears this out.

neither house having suggested the destruction of any part of the claim. If the provision finally enacted be interpreted as limiting only the parity portion, it represents a fair compromise between the positions of the two branches of Congress.

The word "limited" appears for the first time in the final draft of the bill, but its meaning is clarified by the reports of the Conference Committee. That committee first recommended a clause providing that a landlord's claim should "be treated as a claim ranking on a parity with" provable debts "in an amount equal to" three years rent (73rd Cong., 2d Sess., H. R. Rep. No. 1773, p. 2). The House Managers described the effect of this provision as *limiting* rent claims "to an amount not to exceed" three years rent, but they also described the Senate bill as having *limited* rent claims (*ibid.*, p. 5), so that they must have meant in both cases only to refer to a limitation of the parity portion. In the amendment agreed upon in their second report the Conferees substituted the words "but shall be limited to an amount not to exceed [three years rent]" for the words "in an amount equal to [three years rent]" (H. R. No. 1821, p. 2). The words "limited to an amount not to exceed" were the exact language used by the House Managers in explanation of the amendment agreed upon in the first report. Again the word "limited" must have referred only to the parity portion, for in the second report the House Managers again used this word in referring to the original Senate enactment as well as to the provision then recommended, which was finally enacted. Had the Conference Committee intended in either its first or second report to recommend so radical a change from the Senate bill as destroying the non-parity portion of the claim, it is reasonable

to assume that the House Managers would have so stated.

As a matter of fact, the change recommended in the second Conference Report was desirable in order to make clear that a landlord's claim was not to be allowed on a parity "in an amount equal to" three years rent in case the total injury or damage actually proven was less than that amount.

The Court of Appeals ignored the circumstances just described because of the significance which it attributed to the omission from the final bill of the clause contained in the Senate bill expressly subordinating the balance of the landlord's claim over one years rent to provable debts (R. 153). That clause provided merely for the *subordination* of the excess claim, *not for its allowance*; it was mere surplusage, since without its inclusion the balance of the claim over one years rent was required to be subordinated to provable debts, in view of the express provision that the claim should not be allowed on a parity with provable debts, except up to an amount equal to one years rent. The fact that its omission was first recommended in the first Conference Report, which obviously referred to a limitation only of the parity portion, demonstrates that the omission did not have the significance attributed to it.

B: *The underlying purpose of the statute.*

The purpose of the statute was to provide a practical means of enabling embarrassed corporations to continue business in reorganized form. To this end, the definition of creditors is couched in broad terms and the statute provides, in subdivision (h), that the debtor and its assets shall be freed of all liabilities except such as may be specially reserved (*supra,* p. 12). To construe the statute as not providing for the

reservation in priority to stockholders of any valid claims not presently allowable would, as we show below (p. 23), raise grave doubts of its constitutionality. But the attainment of the dominant purpose of the statute—effective reorganization—requires that, so far as practicable, claims should be presently liquidated and allowed, rather than reserved. Therefore, it is not likely that Congress, which undoubtedly knew of the existence of the large lease obligations of many embarrassed corporations, intended that such obligations should be provided for by reservation rather than by present allowance.

C. *The method of liquidation adopted is sufficiently reliable to support the allowability of the entire claim.*

The formula adopted by the Court of Appeals for the measurement of the petitioners' claim—the difference between the total rent reserved, discounted, and the appraised value of the remaining term—is the only method ever followed or even suggested for determining damages for loss of future rent* and is the method uniformly used by the English courts** under the similar provisions of the English bankruptcy statutes,*** irrespective of the type of covenant con-

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* *Leo* v. *Pearce Stores Co.*, 54 F. (2d) 92, 57 F. (2d) 340; *McGraw* v. *Union Trust Co.*, 135 Mich. 609; *Kalkoff* v. *Nelson*, 60 Minn. 284; *In re Reading Iron Works*, 150 Pa. St. 369; *Curran* v. *Smith-Zollinger Co.*, 18 Del. Ch. 220.

** *Ex Parte Blake*, 11 Ch. Div. 572; *Ex Parte Llynvi Coal & Iron Co.; In re Hide*, L. R. 7 Ch. App. 28; *Ex Parte Leather Sellers' Co.*, 3 Morrell 126; *In re Panther Lead Co.* [1896] 1 Ch. Div. 978; *In re Carruthers*, 15 Reports 317, 2 Mansons 172.

*** 4 and 5 Geo. V., c. 59; 46 and 47 Vict., c. 52, Sec. 55(7).

> "We take our bankruptcy system from England, and we naturally assume that the fundamental principles upon which it was administered were adopted by us when we copied the system. * * *" (*Sexton* v. *Dreyfus*, 219 U. S. 339, 344; see also *Willis* v. *Eastern Trust and Banking Co.*, 169 U. S. 295, 307.)

tained in the lease. It is a basis "familiar and fair" when agreed to by the parties (*William Filene's Sons Co.* v. *Weed*, 245 U. S. 597, 602) and "the best means at hand" (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 66 F. [2d] 470, 471). Nevertheless, the Court of Appeals felt that the method is not entirely reliable, due to the difficulty of prophesying the "future value" of realty (R. 153).

But the rental value of real property for a future term is a present fact, not depending on prophecy or future valuation. The problem is merely to ascertain the amount for which the property could be rented *at the present time* for a given term of years. In some cases expert testimony must be resorted to, but that does not depend on the gift of prophecy; it represents, rather, an opinion of one qualified to speak as to a present fact. And expert opinion is not the only or always the best evidence of rental value: if the landlord, exercising reasonable diligence, has succeeded in re-renting the property for the balance of the term, that fact would constitute the best evidence (*Curran* v. *Smith-Zollinger Co., supra*).

This Court will take judicial notice that leases of real property are made every day in the ordinary course of business. Every such lease is made for a future term and many are made for very long terms.* A fact which business men ascertain and rely on every day in the course of their usual business activities cannot be as unreliable as the Court of Appeals appears to consider it.

The method of liquidation adopted does not involve an attempt to forecast either the amount of rents which a landlord will lose over the remainder

* The petitioners' predecessors and the debtor in the case at bar made such a deal in 1926 when one agreed to pay and the other agreed to accept an average annual net rental of $11,000 for the property here involved, over a period of twenty years.

of the term, or what the rental value of the property for shorter periods would be at different dates over the remainder of the term. As the Court of Appeals said, the same measure must be used as in cases of breach of an executory contract for chattels, or the claim cannot be measured at all. The computation of damages in such cases is not influenced by the probability that the actual loss may turn out to be greater or less, or even by the known fact that, because of some circumstance intervening the breach and the award, the predicted loss has actually been turned into a profit (*In re Susquehanna Silk Mills*, 10 F. Supp. 787, aff'd 77 F. [2d] 1015).

Congress did not "circumscribe" the use of the formula to "the near future" or fix a period of "four or five years" "as the maximum forecast which it would be safe to act on", as the Court of Appeals said Congress *might have done* (R. 153-4). On the contrary, the statute, even as interpreted by the Court of Appeals, requires the formula to be used in respect of the entire balance of the term, however long that may be, and requires that the result be adhered to, provided it does not exceed the arbitrary maximum. If the formula had produced a result less than three years rent, the petitioners would have been bound by it.

POINT II.

If the balance of the claim over three years rent is not presently allowable the statute requires that the petitioners' rights under the covenant of indemnity, to the extent they turn out to exceed the amount of the allowed claim, be preserved in priority to stockholders.

Even if the Court of Appeals were correct in holding that the balance of the claim over three years rent was not presently allowable, that would not require or even support the conclusion, to which the Court of Appeals passed without discussion, that the petitioners' rights were intended to be extinguished for the benefit of stockholders. The limitation provision at the very most relates only to the *allowability* of *claims.* Other provisions of the statute (*supra,* p. 12) expressly recognize that some *liabilities* must be *reserved.* There is not one word in the statute which requires the discharge of a landlord's claim over three years rent *for the benefit of stockholders,* or which forbids its reservation *in priority to stockholders.*

Finally, if the entire claim is not presently allowable, the interpretation which we are now urging is required in order to avoid raising grave doubts as to the constitutionality of the statute (*Interstate Commerce Comm.* v. *Oregon-Washington R. & Nav. Co.,* 288 U. S. 14; *Linder* v. *United States,* 268 U. S. 5) and to avoid the harsh and arbitrary inequalities produced by a contrary interpretation* (*Knowlton* v. *Moore,* 178 U. S. 41, 76-77; *United States* v. *Kirby,* 7 Wall. 482, 486). The Court of Appeals itself expressed doubts as to the constitutionality of the stat-

* See *infra,* page 26.

ute as applied to certain landlords' claims (R. 156). The limitation provision is not divisible; it was designed to apply alike to all landlords' claims. Thus these admitted doubts require the interpretation here urged (*cf. Illinois Central R. R. Co.* v. *McKendree,* 203 U. S. 514, 528; *The Employers' Liability Cases,* 207 U. S. 463, 496-501, 504).

POINT III.

The limitation provision, as interpreted by the Court of Appeals, is unconstitutional.

Congress was without power to deprive the petitioners of their fundamental rights as creditors for the benefit of stockholders. The bankruptcy clause of the Constitution authorizes no such legislative repeal of fundamental law and, even if within the general scope of the bankruptcy power, the attempted exercise of the power falls under the prohibition of the Fifth Amendment.

A. *The bankruptcy clause.*

While it is conceded that the bankruptcy power of Congress extends to whatever is necessary or reasonably adapted "under modern conditions to deal adequately with the relationship existing between embarrassed debtors and their creditors" (*Campbell* v. *Alleghany Corp.* 75 F. [2d] 947, 955, cer. den. 296 U. S. 581), the arbitrary extinguishment of a portion of landlords' claims for the benefit of stockholders cannot be supported as a valid exercise of that power.

There was nothing in the practical situation with which Congress was dealing in the enactment of Section 77B (see *Duparquet etc. Co.* v. *Evans,* 297 U. S. 216) which required the legislative repeal of the

fundamental principle that the priority of creditors (however contingent their claims may be) over stockholders could not be evaded by any form of corporate reorganization (*Northern Pacific Ry. Co.* v. *Boyd, supra; Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.*, 271 U. S. 445; *Howard* v. *Maxwell Motor Co., Inc., supra*). The Court of Appeals itself has recognized the controlling effect of the *Boyd* case in reorganization proceedings under Section 77B (*In re New York Railways Corp.*, 82 F. [2d] 739).

Even if the inherent nature of claims justifies their partial exclusion from present allowability on a parity with other debts, that does not necessitate the extinguishment of the unallowable portion of the claims for the benefit of stockholders. Contingent claims may be allowed in subordination to other debts or reserved in priority to the interest of stockholders and corporations may be reorganized effectively without according stockholders a participation at the expense of a single class of creditors.

Nor is the provision reasonably adapted to the object in view—effective reorganization. There is no relation whatever between the amount of three years rent (fixed many years ago) and the present value of an agreement to indemnify against loss of rents during a term which, as in the case at bar, has fourteen years to run. The limitation provision does not provide a method of liquidation of landlords' claims, but requires an actual ascertainment of the total claim before the limitation, whatever it may mean, may be applied.*

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* Compare *Norman* v. *B. & O. R. Co.*, 294 U. S. 240, in which the abrogation of private contracts was upheld as reasonably adapted to the effective exercise of certain powers of Congress, with the exercise of which such contracts interfered.

The only ground on which the Court of Appeals thought the limitation to three years rent had a "rational relation to the end to be achieved" was that it ordinarily would permit a landlord to prove his losses for "four or five years" which the Court thought was "a period which Congress *might* well fix as the maximum forecast which it would be safe to act on" (R. 154). To this assumption there are several answers: (1) the limitation provision does not restrict the liquidation of landlords' losses to any particular period; (2) the liquidation of landlords' claims does not involve forecasting *future* values of real estate; (3) other claims equally or more difficult of liquidation are allowable in full; and (4) if claims may not be liquidated properly, there is no reason for extinguishing them for the benefit of stockholders.

B. *The due process clause.*

The Court of Appeals failed to understand the precise ground of the petitioners' attack on the constitutionality of the statute under the due process clause, saying (R. 153) that the petitioners' position "presupposes that the appraisal of the future value of real estate is so reliable a basis * * * that Congress was obliged to treat it as good against shareholders."

The petitioners did not urge that the statute was unconstitutional if not requiring the present allowance of the entire claim measured by the formula adopted or by any other formula. (It should be noted that the court and not Congress prescribed the use of the formula.) The petitioners' position is that, if their claim is not presently allowable in excess of three years rent, then the failure of the statute to preserve as against stockholders their right

to indemnity, to the extent that it turns out to exceed three years rent, renders the statute unconstitutional. Their complaint is that their contract rights have been appropriated by legislative decree for the benefit of the stockholders, and that the "truncated substitute" measured by a "piepowder standard" is arbitrary, discriminatory and not compensatory.

(1) The limitation provision is arbitrary and discriminatory.

The inequalities and arbitrary discrimination produced by the statute are not incidental, occasional or only remotely possible, but "inevitable and profound" (*Knowlton* v. *Moore, supra*).

It is only theoretically possible—and then only by purest accident—that the provision can operate equally as among landlords similarly situated. As the table printed on the opposite page shows, the provision may—almost must—operate unequally between two landlords even where the amounts of three years rent are identical; even where the unexpired terms of the leases are identical; even where the rental values of the properties are identical; and even where any two of these three elements are identical, or where the total damages, or the respective ratios of total damage to total rent reserved, are identical.*

In every case, irrespective of the identity of all other factors, the determining factor is three times the amount of the annual rent which happens to have been agreed upon when the lease was made, perhaps many years ago. Under that standard, one landlord's loss may be allowed for five years while the losses

* Similar inequalities result if the landlord's damage is considered to be, not the difference between rental value and rent reserved, but the actual loss ascertained at the end of the term.

	A		B		C		D		E		F	
Unexpired term	10 yrs.		10 yrs.		10 yrs.		6 yrs.		4 yrs.		4 yrs.	
Annual rent	$10,000		$10,000		$12,000		$12,000		$18,000		$15,000	
Total rent reserved		$100,000		$100,000		$120,000		$72,000		$72,000		$60,000
Annual rental value	8,000		4,000		4,000		4,000		6,000		3,000	
Total rental value		80,000		40,000		40,000		24,000		24,000		12,000
Total damage		20,000		60,000		80,000		48,000		48,000		48,000
Allowable claim		20,000		30,000		36,000		36,000		48,000		45,000
Destroyed claim		none		30,000		44,000		12,000		none		3,000

(N. B. The above figures are regardless of discount. Substantially similar results would be obtained if the figures for *Total rent reserved* and *Total rental value* were adjusted at the same rate of discount.)

of another are allowed for twenty years. A more arbitrary, unrelated standard could scarcely be imagined. It necessarily produces wholesale inequalities.

The Court of Appeals, although recognizing the gross inequalities produced by the statute as among different landlords, upheld the statute by a curious process of reasoning: the court thought (R. 154) that if Congress had limited landlords' claims to their *losses* for four or five years, *that would have been* reasonable, in view of the supposed unreliability of the formula used for measuring their losses; since ordinarily the limitation of claims to three years rent would permit landlords to prove their losses for at least four or five years, the complaint against the statute is merely that when a landlord's "losses are large he is not treated equally with those whose losses are small". The court concluded that since "no lessor is unjustly treated as against his lessee, this is a complaint to which we are not disposed to lend an auspicious ear", because "nobody should be shocked that in a class of claims like these, so inherently uncertain, a piepowder standard is chosen, even though it operates unevenly as unquestionably it does." The court also suggested that only "the lessee" could complain that some landlords might recover their losses for more than five years and that the lessee could not make this complaint because "he [*sic*] is getting a discharge upon a payment which he cannot show is too great until the occasion is past".

The Court of Appeals ignored the realities of the situation. It is inherent in any scheme of reorganization that every member of each class of creditors and stockholders should receive ratably equal treatment with his fellows in that class. But, under the statute as construed below, as we have shown, only

by the merest accident can any two landlords receive treatment ratably proportionate to their losses, whether presently appraised or subsequently ascertained. That is a complaint, therefore, which should be available to any landlord who does not participate to the full extent of his actual loss.

Moreover, the remarks of the Court of Appeals are relative only to a statute which Congress *might have enacted,* if it had desired to limit all landlords' losses to four or five years—not to the statute actually enacted (see *supra,* p. 28).

Even if ratably equal limitation of landlords' claims would be valid, that should not deprive any landlord of the right to complain that the provision actually enacted does not treat similarly all persons similarly situated but arbitrarily discriminates among members of the same class among whom there is no legal basis for distinction.

Moreover, the court's view that "no lessor is unjustly treated as against his lessee" was based entirely upon the assumption that a rough standard of justice must be applied because of the supposed difficulty of ascertaining the "future value" of real estate. To this there are two answers: first, it is a difficulty which affects only the question of whether the entire claim is *presently allowable* (*supra,* p. 22), and second, it is no difficulty even in that connection (*supra,* p. 19).

The statute produces other inequalities and arbitrary discriminations which the Court of Appeals entirely ignored.

The provision discriminates against landlords in favor of other creditors whose claims are equally difficult of evaluation. Claims based on contracts for

the future purchase or sale of personal property,* even though having no recognized market value; claims for loss of employment or destruction of earning power;** claims for personal injuries, defamation of character, mental suffering; claims for loss of profits due to patent infringement or unfair competition—these and many others, equally or even more difficult of liquidation, are not restricted for the benefit of stockholders.

Of even greater significance is the fact that there is no limitation on claims arising out of licenses (even where involving the use of realty)† and leases of personal property, contracts for the future purchase or sale of real property,‡ other indemnity contracts, or even *contracts guaranteeing the performance of a lease of real estate including a covenant to indemnify against loss of future rent* (*such a claim is not covered by the limitation provision*).

Even more—the claims of landlords of railroad and municipal corporations and of individuals are

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* The Court of Appeals held that the petitioners' claim should be "liquidated like a claim for breach of an executory contract for chattels." See *In re Susquehanna Silk Mills,* 10 F. Supp. 787, aff'd, 77 F. (2d) 1015. In his opinion in the *Manhattan Properties* case (66 F. [2d] 470) Judge Learned Hand said:

> "Certainly I have no more compunction in assessing the future value of realty, than that of chattels. The periods involved are indeed apt to be longer, but the fluctuations are less rapid."

** *In re Schultz & Guthrie,* 235 Fed. 907.

† *Central Trust Co.* v. *Chicago Auditorium,* 240 U. S. 581.

> "The uncertainties attendant upon any future installments [in that case] were as great as in the case of a covenant to pay rent under a lease." (Learned Hand, *C. J.*, in the *Manhattan Properties* case.)

‡ Judge Learned Hand said in the *Manhattan Properties* case:

> "The uncertainty as to the future value of a fee is no less great than as to the value of sequent terms."

allowable in full under Sections 77, 80 and 74 of the Bankruptcy Act. And in ordinary bankruptcy proceedings, while the landlord's claim is provable under Section 63(a), as amended, only up to one years rent, presumably no greater part of the claim is discharged.

Thus the discrimination against landlord creditors in Section 77B cannot be sustained as a valid classification based on the supposed difficulty of liquidating their claims (*cf. Quaker City Cab Co.* v. *Penna.*, 277 U. S. 389).

(2) The limitation provision deprives the petitioners of their property by legislative decree and without making a fair return.

The provision operates automatically—without regard to the condition of the debtor, the extent of the stockholders' equity or any other particular circumstances of the case (*cf. Lowden* v. *Northwestern Nat. Bank & Trust Co.*, 56 S. Ct. 696). The judge has no discretion as to limiting landlords' claims. A landlord is not permitted to show that, under the circumstances, it would be unfair to limit his claim for the enrichment of the stockholders of a solvent corporation. On the question of whether the limitation is fair and equitable under the circumstances the landlord does not have a day in court or a hearing of any kind (*cf. National Surety Co.* v. *Coriell*, 289 U. S. 426; *First Nat. Bank* v. *Flershem*, 290 U. S. 504, 525). "This is not legislation. It is a decree under legislative forms" (*Loan Ass'n* v. *Topeka*, 20 Wall. 655, 664). It is legislative usurpation of judicial power (*Louisville &c. Bank* v. *Radford, supra; Heiner* v. *Donnan*, 285 U. S. 312; *cf. W. B. Worthen Co.* v. *Thomas*, 292 U. S. 426).

The petitioners are given no fair equivalent for the rights of which they are deprived. It probably will be urged that the amount of three years rent presently allowable (on a parity with provable debts) is more than fair compensation for the extinguishment of a right (subordinate to debts now allowable) to be indemnified for loss the amount of which, if any, is not ascertainable until the end of the term. The answer is that each case must be considered on its own merits; and Congress has no power to decree that the substituted remedy is in fact compensatory in every case (*cf. Heiner* v. *Donnan, supra; St. Joseph Stock Yards Co.* v. *United States,* 56 S. Ct. 720, 736-8).

The Court of Appeals reasons (R. 156) that, since the debtor was already in default and subject to dismemberment by its creditors, and the petitioners' claim was not yet suable, their rights against the debtor in the absence of reorganization would have been "no better than if it were out and out insolvent." This reasoning is similar to the argument which was unsuccessfully advanced in the *Boyd* case, that the assets involved in that reorganization were insufficient to pay the mortgage debts, leaving nothing of value for general creditors. In that case this Court said that the superior rights of creditors over stockholders "must be decided according to a fixed principle, not leaving the rights of the creditors to depend upon the balancing of evidence as to" the value of the property, and that if the value of the property justified the issuance of securities to the stockholders "the creditors were entitled to the benefit of that value, whether it was present or prospective, for dividends or only for purposes of control", since "in either event it was a right of property out of which the creditors were

entitled to be paid before the stockholders could retain it for any purpose whatever" (228 U. S. at pp. 507-8).*

Although Section 77B does not contain a severability clause, the unconstitutional provision may be stricken out, leaving the remainder of the statute as operative legislation (*In re Tennessee Publishing Co.*, 81 F. [2d] 463, 468).

Respectfully submitted,

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* There has been no finding that the debtor is insolvent nor has its insolvency even been alleged. There is no basis whatever in the record to support the assumption of the Court of Appeals that the amount of presently enforceable liabilities was so great that dismemberment would have resulted from their enforcement or that if all presently enforceable liabilities had been satisfied a surplus would not have remained which would have constituted a trust fund for contingent creditors such as the petitioners (*Pierce* v. *United States, supra; Block* v. *Bell Furniture Co., supra*). On the contrary, the active participation of a Preferred Stockholders' Protective Committee in the proceedings, as shown by the record, indicates the likelihood that a substantial equity exists over provable debts and the portion of landlords' claims allowable on a parity.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 354.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Petitioners,

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders Protective Committee, *et al.*,
Respondents.

PETITIONERS' REPLY BRIEF.

ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
HENRY L. GLENN,
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Respondents.

ON PETITION FOR WRIT OF CERTIORARI.

PETITIONERS' REPLY BRIEF.

I.

The trustee's answering brief contains the astonishing argument that petitioners have no standing to challenge the constitutionality of the limitation provision because they "have accepted the benefit of the statutory scheme of liquidation".

In *Calhoun* v. *Massie,* 253 U. S. 170, cited by the trustee, the person estopped from attacking the statute in question had actually accepted a payment of money

from the Federal Government, to no part of which would he have been entitled but for the enactment of the statute. *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234, also cited by the trustee, simply held that bank depositors could not withdraw, pursuant to the terms of a reorganization plan adopted and confirmed under a New York statute, a portion of the deposits due them by an insolvent bank, and *afterwards* sue the bank for the balance of their deposits on the ground that the statute pursuant to which the bank was reorganized was unconstitutional.

In the case at bar the petitioners, long prior to the confirmation of a plan of reorganization (one has not even yet been formally proposed) and at the very inception of the proceeding brought by the trustee for the purpose of determining whether the petitioners' claim should be allowed, even in the amount of three years' rent (see Main Brief, pp. 3-4), urged that their entire claim was provable and that, if any part were not provable, it should be reserved as a charge against the assets, and challenged the constitutionality of the limitation provision if construed so as to limit their participation to three years' rent. The petitioners could have done nothing more.

The Special Master refused to pass on the constitutionality of the provision, but the District Court and the Court of Appeals held it constitutional as so construed.

The petitioners have as yet accepted nothing. The trustee's argument thus boils down to the contention that petitioners' inability to appeal from the portion of the order of the District Court partially allowing their claim to the extent of three years' rent constitutes an acceptance of a benefit which now bars them from raising the question of the validity of the

statute, though that question was duly raised before the claim was held to be allowable in any amount.

II.

The trustee argues that the petitioners cannot show at the present time that they are in immediate danger of direct injury because it will not be known until the end of the term whether the amount of three years' rent is equal to or less than the petitioners' actual loss. It is sufficiently shown in the petitioners' main brief that they are in immediate danger of direct injury because by the operation of the limitation provision and the discharge provisions of subdivision (h) of Section 77B, they will be deprived of a present contract right of indemnity. No method of presently evaluating in dollars and cents that contract of indemnity is available to the petitioners, other than the one universally accepted for evaluating landlords' claims (see Our Main Brief, p. 19). But even if the trustee's contention were sound,—that the question of constitutionality cannot be litigated until the amount of the petitioners' actual loss is known, the order entered in the present proceedings clearly should be without prejudice to the petitioners' right to attack the statute at the end of the term. Consequently, in any event, the petition for certiorari should be granted so that the order of the court below may be corrected in this respect.

Respectfully submitted,

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Petitioners,

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Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR PETITIONERS.

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HENRY L. GLENN,
MITCHELL, TAYLOR, CAPRON & MARSH,
Of Counsel.

THE COURT PRESS, N. Y. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 354.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,

Petitioners,

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders Protective Committee, *et al.*,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR PETITIONERS.

OPINIONS BELOW.

The opinion of the District Court appears at page 146 of the record and is not officially reported. The opinion of the United States Circuit Court of Appeals is reported at 85 F. (2d) 35.

JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The order for mandate was entered on July 20, 1936. The petition for certiorari was filed September 10, 1936, and granted October 26, 1936.

QUESTIONS PRESENTED.

This case involves the interpretation and constitutionality of the limitation on landlords' claims in corporate reorganization proceedings under Section 77B of the Bankruptcy Act.*

The petitioners' claim arises out of a lease of real estate between their predecessors, as lessors, and the debtor corporation, as lessee, which, when it still had about fourteen years to run, had been rejected by the debtor's trustee in bankruptcy proceedings in which the 77B proceedings were subsequently instituted. After the rejection of the lease and before the enactment of Section 77B, the petitioners reentered under a covenant (R. 57), which provided that in such case the lease should terminate and the debtor should:

"indemnify the Landlords against all loss of rent

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* Relevant portions of the statute are quoted below at pp. 4-5. The limitation provision provides:

> "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent"

reserved by the lease for a period of three years after the surrender of the premises to the landlord or the landlord's reentry, plus accrued, unpaid rent.

which the Landlords may incur by reason of such termination, during the residue of the term above specified."

The petitioners' claim, measured by the difference between the rent reserved and the present rental value of the premises for the unexpired term, was established by uncontradicted testimony at $87,692.30, subject to appropriate discount.* The courts below allowed the petitioners' claim on a parity with other claims against the debtor, in the amount of $44,377.55, the amount of three years' rent**, but rejected the petitioners' contention that the balance of their claim should be recognized in the reorganization proceedings in subordination to other creditors but *in priority to the debtor's stockholders.* On this state of the case, the following questions are presented:

1. Should the provision of Section 77B limiting landlords' claims be interpreted as limiting only the amount in which the petitioners' claim is allowable on a parity with other debts, permitting the balance of the claim to be allowed in subordination to other debts but in priority to the debtor's stockholders?

2. If the balance of the claim over three years' rent is not presently allowable, even in a subordinate

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* By understanding of the parties, all questions as to discount and interest have been reserved for future determination. The petitioners' claim, even after being discounted on any reasonable basis, still would exceed three years' rent by a substantial amount.

** The term "three years' rent", as used herein, includes accrued unpaid rent up to the date of surrender or reentry, as provided in the statutory formula.

position, are the petitioners entitled to have their rights against the debtor and its assets reserved in priority to the debtor's stockholders, to the extent that their loss turns out to exceed the amount of three years' rent?

3. If the statute is interpreted as restricting the petitioners' right to participate in the reorganization to the allowance of the claim in an amount equal to three years' rent, even although stockholders participate in the reorganization, is the statute to that extent unconstitutional as beyond the power of Congress under the Bankruptcy Clause and in contravention of the Fifth and Tenth Amendments?

THE STATUTE.

Section 77B of the Bankruptcy Act provides:

"Sec. 77B. Corporate Reorganizations * * *.

(b) * * * (10) * * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts * * * or other interest of whatever character. * * *

In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall,

for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry. * * *

(h) Upon final confirmation of the plan, * * * the property dealt with by the plan * * * shall be free and clear of all claims of the debtor, its stockholders and creditors, except such as may consistently with the provisions of the plan be reserved * * *. Upon the termination of the proceedings a final decree shall be entered * * *. Such final decree shall discharge the debtor from its debts and liabilities, and shall terminate and end all rights and interests of its stockholders, except as provided in the plan or as may be reserved as aforesaid. * * *"

(Act approved June 7, 1934, 48 St. 911, Ch. 424, §1; U. S. C. Tit. 11, §207.)

THE FACTS.

The lease to the debtor, covering premises situated in New Jersey, was entered into in 1926 for a term expiring in 1946, at a net annual rental of $10,500 for the first ten years and $11,500 thereafter (R. 46).

On August 29, 1932, the debtor filed its voluntary petition in bankruptcy, was adjudicated and abandoned the premises. On November 14, 1932, the trustee in bankruptcy rejected the lease and abandoned the premises and on the following day the landlords reentered (R. 6, 40), thus terminating the lease (R. 57). The lease obligated the debtor in such event to indemnify the landlords against all loss of rent which they might incur by reason of such termination during the residue of the term (R. 57).

The debtor's petition for reorganization under Section 77B was filed in the bankruptcy proceedings on June 9 and approved on June 14, 1934. The petitioners filed a proof of claim (R. 4) praying that their claim "based upon or arising out of the lease * * * or for injury resulting from the rejection of said lease by the Trustee in Bankruptcy * * * or for damages or indemnity under a covenant or covenants contained in said lease", measured by the difference between the rent reserved and the rental value for the remainder of the term, be allowed on a parity with provable debts to the extent of three years' rent and that the balance be allowed in subordination to provable debts but in priority to the claims or interests of the stockholders of the debtor.

The reorganization trustee objected, asking that the claim be reduced to an amount "limited as provided by the statute" (R. 15).

At the hearing, committees representing preferred stockholders and debentureholders of the debtor objected to the allowance of the claim in any amount (R. 21) on the ground that the petitioners could not sue on the covenant of indemnity until the expiration of the term. Thereupon the petitioners amended the proof of claim so as to pray that, to the extent that any part of the claim should be held not provable,

a charge be reserved against the debtor's assets, at least in priority to any interest accorded to stockholders (R. 25).

The fair rental value of the premises for the balance of the term is $111,545.36 (R. 73). The expert testimony establishing this value was not controverted. The future installments of rent under the lease for the remainder of the term (including taxes and other items payable as additional rent) aggregate $199,237.66.

THE RULINGS BELOW.

The Special Master reported that the petitioners' claim was valid and should be liquidated according to the customary formula of difference between rent reserved and rental value. He found that the total claim, on that basis, would be not less than an amount equal to three years' rent, and he recommended (1) that the claim should be allowed on a parity with provable debts to the extent of three years' rent, to wit, $44,377.55 and (2) that all questions as to the balance of the claim should be reserved until the time of the classification of creditors and the consideration of a reorganization plan (R. 88, 93). The Special Master stated (R. 88):

> "Whether there will be a surplus over and above the amount of provable claims and expenses of administration, how the same is to be distributed and, in fact, the method of payment and manner thereof to the various creditors, will depend upon the classification of creditors and the respective rights of the various interested parties herein. All these matters will only be presented when the time for classification arrives, and when various questions arise in the consideration and the confirmation of any Plan of Reorganization."

The District Court confirmed the Special Master's report "with the exception that the claim as allowed shall represent the extent of claimant's right to participate in these proceedings" (R. 146). The order entered in the District Court (R. 116-118) provided that the report of the Special Master

> "be, and the same is, approved and confirmed, with the exception that the extent of the claimants' right to participate in these proceedings shall be limited to the amount found by said report to be allowable, to-wit, $44,377.55."

On cross appeals, the Court of Appeals affirmed (R. 150).

SPECIFICATION OF ERRORS.

The Court of Appeals erred in holding:

(1) that the limitation provision prohibited the allowance of the balance of petitioners' claim over three years' rent in subordination to provable debts but in priority to the interest of stockholders;

(2) that the limitation provision prohibited the reservation of the petitioners' residual rights in priority to the interest of stockholders;

(3) that the limitation provision as so interpreted was a valid exercise of the bankruptcy power and did not violate the Fifth Amendment;

(4) that the petitioners had no standing to complain that other landlord creditors similarly situated would receive more favorable treatment than the petitioners as a result of the operation of the limitation provision as so interpreted.

SUMMARY OF ARGUMENT.

The limitation provision does not prescribe a short-cut method for liquidating landlords' claims. The statute requires that the landlord's loss over the entire unexpired term be determined by judicial process, without regard to any supposed difficulties of liquidation and before the "limitation" is applied. The formula adopted by the Court of Appeals for the liquidation of the petitioners' claim is the only one used or suggested in the American or English precedents and has been called "familiar and fair" by this Court. It is entirely reliable, since the *present rental value* of *future terms* is a fact ascertained and relied on in daily business activities (I, pp. 12-16).

The limitation provision was intended, not to fix the maximum amount of a landlord's claim, but merely to limit the portion of the claim which is to be treated on a parity with other debts. It was not designed for the benefit of stockholders and should not be interpreted as attempting to overthrow the fundamental principle that even contingent creditors are entitled to resort to the corporate assets in priority to stockholders. Therefore, the balance of the petitioners' claim in excess of three years' rent should be allowed in subordination to other debts but in priority to the interest of stockholders. Such interpretation is consistent with the language of the limitation provision, is indicated by the general structure of the statute, its background, legislative history and underlying purposes, and is required in order to avoid questions as to the constitutionality of the limitation provision (II, pp. 17-28).

If the balance of the claim is not presently allowable, even in subordination to other debts, the statute requires that the petitioners' rights be reserved in

priority to stockholders, to the extent that their loss turns out to exceed the amount of the claim allowed on a parity with other debts (III, pp. 29-30).

As interpreted below the limitation provision is not within the bankruptcy power since it is neither necessary nor reasonably adapted to the end in view—effective reorganization of embarrassed corporations (IV, pp. 32-38). Even if within the general scope of the power, the limitation provision as so interpreted violates the due process clause because of its arbitrary and discriminatory operation and because it deprives the petitioners of their rights by legislative decree (IV, pp. 38-46).

The limitation provision as so interpreted inflicts legal injury upon the petitioners, who have not waived and are not estopped to assert its unconstitutionality (V, pp. 46-51).

The balance of the petitioners' claim over three years' rent should be allowed in priority to the interest of stockholders or the disallowance of such balance should be without prejudice to the petitioners' right to demand appropriate reservation of their rights as against stockholders (VI, p. 52).

ARGUMENT.

The courts below have held that the petitioners' claim, measured by the difference between the future rent instalments, discounted, and the present value of the remaining term, is entitled to recognition in the 77B proceedings, subject only to limitation to an amount equal to three years' rent. The respondents do not challenge that holding, nor have they at any time questioned the rental value of the premises as established by the petitioners' witnesses.

There has been no determination that the debtor is insolvent, nor has its insolvency even been alleged. No evidence was adduced at the hearing as to the value of the debtor's assets or the amount of its liabilities. No plan for the reorganization of the debtor has been proposed.

Nevertheless, the preferred stockholders of the debtor, and the trustee on their behalf, have contended (so far with success) that the debtor's stockholders are entitled to participate in the benefits of whatever reorganization may be effected, without the recognition of more than a fraction of the petitioners' claim, no matter how large may be the "equity" thus created for the stockholders.

The Court of Appeals sustained the limitation of the petitioners' rights for the benefit of the debtor's stockholders solely because of supposed difficulties in liquidating their claim, despite the facts that the statute requires the liquidation of the claim and the court itself selected the formula for its liquidation. The Court of Appeals mistakenly assumed that the liquidation of such claims depends upon prophecy or mere guess-work as to the future rental value of the leased properties, and intimated that Congress may have desired to restrict the period of such forecasting to the near future.

The question of liquidation thus lies at the threshold of the case and we propose to discuss it first, and then address our attention to the interpretation and constitutionality of the limitation provision.

I.

The statute requires that the petitioners' entire claim be liquidated by judicial process: it may be liquidated on a basis "familiar and fair".

The limitation provision does not purport to give every landlord a claim equal to three years' rent. The provision obviously requires that the landlord's claim be liquidated by judicial process; that the result so arrived at, if not in excess of three years' rent, shall be the measure of his claim; but that if such result is in excess of three years' rent, the limitation then shall be applied.

The Court of Appeals stated the correct formula for the measurement of the petitioners' claim as the difference between the total rent reserved, discounted, and the appraised value of the remaining term. As the court pointed out in its opinion, if that method were not adopted, the claim could not be liquidated at all (R. 152).

The formula thus adopted is the only one which has ever been used or even suggested for determining damages for loss of future rent or the present value of a covenant to indemnify against loss of rent.* It is the method uniformly used by the English courts**

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* *Leo* v. *Pearce Stores Co.*, 54 F. (2d) 92, 57 F. (2d) 340; *McGraw* v. *Union Trust Co.*, 135 Mich. 609; *Kalkoff* v. *Nelson*, 60 Minn. 284; *In re Reading Iron Works*, 150 Pa. St. 369; *Curran* v. *Smith-Zollinger Co.*, 18 Del. Ch. 220; *cf. Bowditch* v. *Raymond*, 146 Mass. 109.

** *Ex Parte Blake*, 11 Ch. Div. 572; *Ex Parte Llynvi Coal & Iron Co.; In re Hide*, L. R. 7 Ch. App. 28; *Ex Parte Leather Sellers' Co.*, 3 Morrell 126; *In re Panther Lead Co.*, [1896] 1 Ch. Div. 978; *cf. In re Carruthers*, 15 Reports 317, 2 Mansons 172.

under the similar provisions of the English bankruptcy statutes,* irrespective of the type of covenant contained in the lease, and even though the English statute, like Section 77B, contains no direction as to the method of liquidation.

In the case at bar, the Court of Appeals felt that when the formula is agreed to by the parties, it is thoroughly reliable and even entitled to protection under the constitution (R. 156). It is difficult to perceive how the formula can be more reliable when provided for by agreement than when adopted by the courts as the only judicial method available. This Court, when holding in *Wm. Filene's Sons Co.* v. *Weed*, 245 U. S. 597 (at p. 602), that a lease covenant prescribing the use of the formula liquidates the landlord's damages on a basis "familiar and fair", cited cases in which the courts had applied the formula although no method of liquidation had been agreed upon.

The decisions of this Court in *Manhattan Properties, Inc.* v. *Irving Trust Company*, 291 U. S. 320, and *Miller* v. *Irving Trust Company*, 296 U. S. 256, that landlords' claims based on similar covenants of indemnity were not provable in bankruptcy before the 1934 amendment to Section 63(a), are not con-

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* 46 and 47 Vict., c. 52, provided:

"Any person injured by the operation of a disclaimer under this section shall be deemed to be a creditor * * *."

See also 4 and 5, Geo. V, c. 59.

"We take our bankruptcy system from England, and we naturally assume that the fundamental principles upon which it was administered were adopted by us when we copied the system. * * *" (*Sexton* v. *Dreyfus*, 219 U. S. 339, 344.) See also *Willis* v. *Eastern Trust and Banking Co.*, 169 U. S. 295, 307.

trolling. The statute before the Court in those cases, unlike Section 77B, did not expressly recognize such claims or require their liquidation.*

Although approving the use of the customary formula for the liquidation of the claim, the Court of Appeals felt that it is not entirely reliable, due to the difficulty of prophesying the "future value" of realty (R. 153). This feeling was unjustified. In applying the formula, the problem is not to guess the future rental value of the property for successive short periods over the balance of the term, but merely to ascertain the amount for which the property could have been rented, at the date as of which the formula is applied, for a single period running until the end of the term stipulated in the old lease. The *present rental value* of real property for a *future term* is an existing fact the determination of which does not depend on prophecy or future valuation. It is true

* In *Miller* v. *Irving Trust Company*, the covenant required the tenant to pay to the landlord, on each rent day, the difference between the amount of rent reserved in the lease and whatever amount may have been collected by the landlord on a reletting. This Court, in holding that the landlord was not entitled (before the amendment) to prove a claim measured by the difference between rent reserved and rental value, apparently took the view that the landlord was not required to relet at current rental values and, therefore, current rental values could have no relevancy in the adjudication of his rights. In the case at bar, the debtor has agreed to *indemnify* the landlord against *loss* of rents. Under such a covenant, the landlord is required to act diligently and prudently in reletting the property; if he declines a fair offer at the current rental value, he nevertheless is charged with the amount he could have obtained in ascertaining the loss that he is entitled to recoup from the tenant (*Lenco, Inc.* v. *Hirschfeld*, 247 N. Y. 44, 50; *Fitch* v. *Armour*, 14 N. Y. S. 319; *Edmands* v. *Rust & Richardson Drug Company*, 191 Mass. 123; see, also, *International Trust Company* v. *Weeks*, 203 U. S. 364; *cf. Curran* v. *Smith-Zollinger Company*, 18 Del. Ch. 220). Consequently, under such a covenant the recognition of a claim measured with reference to current rental values does not require a material departure from the terms of the contract.

that in some cases expert testimony must be resorted to, but that does not depend on the gift of prophecy; it represents, rather, an opinion of one qualified to speak as to a past or present fact. And expert opinion is not the only or always the best evidence of rental value; if the landlord, exercising reasonable diligence, has succeeded in rerenting the property for the balance of the term that fact would constitute the best evidence (*Curran* v. *Smith-Zollinger Co., supra*).

Nor does the use of the formula involve an attempt to forecast the amount of rent the landlord will lose over the remainder of the term. As the Court of Appeals said (R. 152), the method adopted is the same as is used in cases involving breaches of executory contracts for chattels and that method must be adopted or the claim cannot be measured at all. The computation of damages for breach of an executory contract for chattels is not influenced by the probability that the actual loss may turn out to be greater or less, or even by the known fact that, because of some circumstance intervening the breach and the award, the predicted loss actually has been turned into a profit (*In re Susquehanna Silk Mills,* 10 F. Supp. 787, aff'd 77 F. [2d] 1015).

This Court will take judicial notice that leases of real property are made every day in the ordinary course of business. Every such lease is made for a future term and many are made for very long terms. The petitioners' predecessors and the debtor in the case at bar made such a deal in 1926 when one agreed to pay and the other agreed to accept an average annual net rental of $11,000 for the property here involved, over a period of twenty years. In every such transaction, the *present rental value* for a *future term* is determined as a practical matter

and for practical purposes. A fact which business men ascertain and rely on every day in the course of their usual business activities cannot be as unreliable as the Court of Appeals appears to consider it.

The Court of Appeals was wrong in intimating that Congress may have intended or desired to "circumscribe" the use of the formula to "the near future" or to fix a period of "four or five years" "as the maximum forecast which it would be safe to act on" (R. 153-4). The fact is that Congress did not do so. The statute, even as interpreted by the Court of Appeals, requires the landlord's entire claim to be measured with reference to the current rental value of the property over the *entire remainder of the term* (fourteen years, in the case at bar), and requires that the result so arrived at be adhered to, provided only it does not exceed the arbitrary maximum of three years' rent. Clearly, if the formula adopted had produced a result less than three years' rent the petitioners would have been bound by it.

We conclude, therefore, that the method of liquidation adopted by the Court of Appeals is the proper method for the measurement of the petitioners' claim; that Congress intended that the entire claim for the entire balance of the term be so measured and liquidated, however long the "forecast" might be; and that Congress intended that the method of liquidation so adopted should fix the extent of the petitioners' rights to participate in the reorganization, subject only to the arbitrary limitation.

II.

The balance of the petitioners' claim over three years' rent is allowable in subordination to provable debts but in priority to the interests of stockholders.

Despite the fact that the petitioners' claim was not provable in the prior bankruptcy proceedings of the debtor and was contingent and unliquidated, the petitioners were creditors. Their contract right to look to the debtor or its assets for indemnity against loss of rent would not have been extinguished by a discharge in bankruptcy; or by the voluntary liquidation of the debtor (*Pierce* v. *United States,* 255 U. S. 398); or by insolvency or winding up proceedings under the law of New Jersey, the state of incorporation of the debtor (*Block* v. *Bell Furniture Co.,* 111 N. J. Eq., 551); or by any form of reorganization (*Northern Pacific Railroad Company* v. *Boyd,* 228 U. S. 482; *Howard* v. *Maxwell Motor Co., Inc.,* 269 Fed. 292, aff'd 275 Fed. 53; see *Landlords' Claims in Reorganization,* 42 Yale L. J., 1003, 1015-1026).*

No statute theretofore enacted "for the relief of debtors" or for any other purpose had attempted to upset the established principle under which even contingent creditors are protected as against stockholders.** The controlling canon of statutory construction to be applied in such a case was announced by

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* *Block* v. *Bell Furniture Co.* and *Howard* v. *Maxwell Motor Co., Inc.* involved landlords' claims for loss of rent.

** See, for instance, *Kalkoff* v. *Nelson, supra; Block* v. *Bell Furniture Co., supra; In re Mechanics Trust Co.,* 119 N. J. Eq. 141; N. Y. Insurance Law, Sec. 425.

Chief Justice Marshall in *United States* v. *Fisher*, 2 Cranch. 358, at page 388:

> "Where rights are infringed, where fundamental principles are overthrown, where the general system of the laws is departed from, the legislative intention must be expressed with irresistible clearness, to induce a court of justice to suppose a design to effect such objects."

The limitation provision contains no clear expression of a design to benefit stockholders at the expense of contingent creditors. The language may be ambiguous, but it is at least susceptible of an interpretation giving the full amount of a landlord's loss priority over the debtor's stockholders. Moreover, the background, legislative history and underlying purposes of Section 77B indicate that Congress had no intention of attempting to overthrow the fundamental principles above referred to.

Finally, the interpretation which we urge should be adopted in order to avoid questions as to the constitutionality of the statute (*infra*, pp. 31-46).

A. *The Background and Purpose of the Limitation on Landlords' Claims.*

In arriving at the correct interpretation of the limitation provision, it is important to consider the time when and the circumstances under which the special provisions relating to landlords' claims were inserted in Section 77B and, by amendment, in the general Bankruptcy Act.

Manhattan Properties Inc. v. *Irving Trust Company, supra*, involving the provability in bankruptcy of landlords' claims for loss of future rents, was

argued and decided in this Court while the bill which eventually became Section 77B was pending in Congress.

The petitioners in that case called attention to the growing epidemic of chain store bankruptcies being engineered for the purpose of obtaining relief from burdensome leases and pointed to recent articles in legal periodicals deploring the situation.*

Counsel for Irving Trust Company stressed the superior rights of general creditors. They stated that "banks, merchandise creditors and others in granting credit have assumed that, in case of any insolvency, the tangible assets of the borrower would be available for such creditors to the exclusion of landlords asserting claims for loss of future rent." They stated that to overturn the existing practice would "require banks, manufacturers, merchants and others extending credit to reconsider and revise all existing lines of credit" which might "well precipitate bankruptcies which would not otherwise occur".

Counsel for the National Association of Credit Men and counsel for a committee of merchandise creditors filed briefs as *amici curiae,* and urged the same considerations. None of those counsel advanced for the consideration of this Court any rights or equities of chain store *stockholders* over landlord creditors. On the contrary, it was well understood that, if landlords' claims were held not provable they would not be discharged, but would continue as valid, subsisting obligations of the bankrupt corporations, and that the landlords' priority over stockholders could not be defeated by any form of corporate reorganization

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* See, for example, 42 Yale L. J. 1003; 33 Col. L. R. 231; 7 Univ. of Cinn. L. R. 164.

effected in connection with the bankruptcy proceedings.*

The problem before Congress was to put an end to the intolerable situation in which many landlords had been placed, without at the same time injuring the commercial credit of tenants by too liberal treatment of landlords. That object could be and was accomplished easily in the amendment to Section 63(a) enacted as a part of the bill containing the corporate reorganization provisions, by limiting the extent to which landlords' claims should be provable, leaving any excess claims both non-provable and non-dischargeable and fully protected by "the rule in the *Boyd* case."

We submit that the same object, and nothing more, was intended to be accomplished by the limitation on landlords' claims in corporate reorganization proceedings. There is no evidence that Congress desired to benefit stockholders. On the contrary, on January 6, 1933, Representative Celler made some scathing remarks on the floor of the House as to the pending bankruptcy proceedings of this debtor, United Cigar Stores Company of America, and other chain stores (76 Cong. Rec., Pt. 2, p. 1360). Representative Celler said that he was introducing a bill "to prevent

* In a footnote at page 49 of the brief for Irving Trust Company in the *Manhattan Properties* case the following statement was made:

> "Petitioner's brief (p. 33) argues that under the existing practice a corporate tenant with sufficient assets to pay all other classes of creditors may, for the purpose of escaping liability on leases, file a voluntary petition in bankruptcy. The argument assumes that the corporation or its stockholders can through bankruptcy benefit at the expense of those having prior rights. In this connection see *Northern Pacific Railway Co.* v. *Boyd*, 228 U. S. 482; 'Landlord Claims in Reorganization' by William O. Douglas and Jerome Frank, 42 Yale Law Journal 1003 (1933)."

the recurrence of such scandals as grew out of the United Cigar Stores bankruptcy" by making landlords' claims provable. While that bill was not enacted, its provisions were very similar to the landlord provisions of Section 77B as originally passed in the House (*ibid.*).

This historical background of the legislation now before the Court cannot be ignored. It discloses the situation with which Congress was required to deal and the evils which it desired to remedy. The resulting enactment should not be interpreted as accomplishing more far-reaching results, unless required by the clearest and most compelling language.

B. *The Language and Legislative History.*

The general structure of Section 77B supports the interpretation that the limitation provision limits only the part of the claim allowable on a parity with provable debts, and was not intended to confer a windfall on stockholders.

Subdivision (b) defines "creditors" as including "all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act" and defines "claims" as including "debts * * * or other interest of whatever character". The statute then specifically provides that any person injured by the rejection of an unexpired lease in the reorganization proceedings or in prior proceedings shall "*for all purposes of* this section and of *the reorganization plan,* its acceptance and confirmation, be deemed to be a creditor". These provisions clearly establish the landlord's status as a creditor to the full extent of his injury, damages or right to indemnity. The

intent to restrict that status by other provisions can be shown only by equally clear and unambiguous language.

There is no language anywhere in the statute which, in express terms, limits the landlord's status as a creditor. The limitation provision is contained in the succeeding sentence which deals only with the relative rank of his claim as compared with other debts. It is merely a subordinate proviso clause which should be read as limiting only the sentence to which it is attached (*cf. United States* v. *Morrow,* 266 U. S. 531, 535). To interpret it as restricting the landlord's general status as a creditor would make it conflict with and override the earlier provisions quoted above.

Indeed, the fact that the limitation provision requires that the landlord's claim be treated on a parity with provable debts, subject to limitation in amount, indicates the positive intention of Congress that the balance of the claim, if any, be accorded subordinate treatment. Nowhere else in the statute is the rank or priority of claims prescribed (except the priority of certain unsecured claims over mortgage liens). Therefore, in the absence of liens or statutory or contractual priorities, all claims allowed in the reorganization proceeding rank equally, whether or not they would be provable under Section 63(a). The limitation provision was designed to deny to a portion of landlords' claims the rank they otherwise would have enjoyed by virtue of the general operation of the statute. But if it is interpreted as fixing the amount of such claims for all purposes, the reference to parity is useless verbiage, as the Court of Appeals admits (R. 153).

The legislative history also supports the interpretation here urged.

The bill, as originally passed by the House, allowed landlords' claims in full, without restriction as to either amount or rank (H. R. 5884, June 2, 1933, p. 10).

The limitation provision was originally inserted in the bill on the floor of the Senate (H. R. 5884, May 7, 1934, p. 11) and provided merely that the landlord's claim "shall not be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this Act, except up to an amount equal to [one year's rent], but the balance, if any, of such claim shall be subordinated in rank to debts so provable". Quite clearly that provision was concerned only with the rank, and not at all with the amount, of the landlord's claim. The history of the development of the provision into its final form does not indicate that its original purpose and scope were intended to be broadened.

The House refused to accept the Senate amendment and the bill went to conference. The difference which was required to be compromised in conference related only to the amount allowable on a parity with provable debts, *neither the House nor the Senate having suggested the destruction of any part of the claim.* If the limitation provision as finally enacted be interpreted as limiting only the parity rank of landlords' claims, it represents a fair compromise between the positions of the two branches of Congress.*

The interpretation of the statute urged by the respondents requires us to assume that the Conferees took it upon themselves to eliminate from the bill the unlimited recognition of landlord's claims which already had been agreed to by both houses. The as-

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* The House bill—full parity.
The Senate amendment—one year's parity.
The compromise—3 years' parity

sumption is entirely unjustified; there was no reason for the Conferees to make such a radical departure, and there is nothing in the Committee Reports or elsewhere in the legislative history which indicates their intention of doing so.

The respondents' argument emphasizes the one word "limited". But the question at issue is not as to the meaning of that word, but is merely whether the *amount* of landlords' claims or their ***rank*** was intended to be limited. This can be determined from the reports of the Conference Committee which framed the limitation provision as finally enacted.

On May 24, 1934, the Conference Committee submitted a report (H. R. Rep. 1773, 73d Congress, 2d Sess., p. 2) in which it recommended a compromise clause providing merely that a landlord's claim should "*be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this act in an amount equal to*" three years' rent. In their explanation of the clause thus agreed upon in conference, the House Managers made the following statement (*ibid*, p. 5):

> "Amendment No. 14: Under the House Bill, executory contracts, including claims for future rent, are made provable claims for the purposes of this section. *The Senate Amendment limited claims for future rent* to an amount equal to the rent reserved by the lease for 1 year.
>
> "The amendment agreed to by conference makes any person injured by the rejection of an executory contract or unexpired lease of real estate a creditor for the purposes of this section. *The claim of the landlord* for injury resulting from loss of future rents *is limited to an amount not to exceed the rent* reserved by the lease *for*

3 years next succeeding the date of surrender of the premises or the date of reentry of the landlord, whichever first occurs, plus unpaid rent accrued up to such date of surrender or reentry of the landlord * * *." (Italics ours.)

It will be observed that this statement described the Senate amendment as *limiting* landlords' claims *to an amount equal to* one year's rent, although the Senate amendment clearly permitted any balance over one year's rent to be allowed in subordination to other claims. The House Managers also described the language then being recommended by the Conferees as *limiting* landlords' claims *to an amount not to exceed* three years' rent, although such language did not contain the word *"limited"* but merely provided that landlords' claims should be *treated on a parity* with provable debts *"in an amount equal to"* three years' rent. It is quite clear that the House Managers could have intended, in both instances, to refer only to a *limitation of the parity ranking* of landlords' claims as against other creditors.

The Conference Report above referred to was superseded, on May 29, 1934, by a second Conference Report (H. R. No. 1821, p. 2) in which the Conferees recommended the provision which was finally enacted and which differed from the provision they had first recommended by the substitution of the words "shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this act, but shall be limited to an amount not to exceed [3 years' rent]" for the words "shall be treated as a claim ranking on a parity with debts which would be provable under section 63(a) of this act in an amount equal to [3 years' rent]". The words *"limited to an amount not to exceed"* were taken *verbatim*

out of the statement of the House Managers submitted with the first Conference Report and those words must have been intended to retain the meaning in which they already had been used. There is nothing to indicate that the words were intended to have a broader meaning. On the contrary, the statement of the House Managers submitted with the second Conference Report contains identically the same explanation of the effect of the original House bill, the effect of the Senate amendment and the effect of the amendment then being recommended, as they had submitted in connection with the first Conference Report.

The explanation of the change made in the limitation provision after the Conference Committee had made its first report is doubtless as follows. The Conferees must have felt that the provision first recommended by them (a claim "shall be treated as a claim ranking on a parity * * * *in an amount equal to*" three years' rent) might lead to the contention that every landlord should have a claim equal to three years' rent, without being required to establish the amount of his claim by proof. It was in order to avoid such a contention and to make it clear beyond dispute that every landlord would be required to prove the amount of his claim, that the language first recommended was abandoned.

If the Conference Committee had intended, in either its first or second report, to go beyond the conflict between the original House and Senate provisions and to recommend so radical a change as the destruction of any part of the landlord's claim, it is reasonable to assume that the House Managers would have made some statement to that effect.

The Court of Appeals refused to be guided by the legislative history outlined above because of the significance which it attributed to the omission from the final bill of the clause contained in the Senate bill expressly subordinating the balance of the landlord's claim over one year's rent to provable debts, apparently believing that that clause had expressly provided for the subordinate *allowance* of the balance of the claim and that its final omission must have reflected a contrary intention (R. 153). But the subordination clause did not provide expressly for the *allowance* or recognition of the balance of the landlord's claim; it provided merely for its *subordination*. The clause was mere surplusage, since without its inclusion the balance of the claim over one year's rent was allowable but was required to be subordinated, in view of the express provision that the claim should not be treated on a parity, except up to an amount equal to one year's rent. That the clause was omitted only because it was deemed surplusage is shown by the fact that its omission was first recommended in the first Conference Report in which a substitute provision was recommended which, as we have shown, clearly limited only the parity ranking of landlords' claims. Thus, the Conference Committee, in recommending the omission of the subordination clause, could not possibly have intended the omission to have the significance which the Court of Appeals attributed to it.

Nowhere in the statute can be found the clear and compelling language which is required in order to support the harsh interpretation urged by the respondents. Nowhere in the background or legislative history of the statute can be found even an intimation of an intention by Congress to enact legislation

"for the relief of stockholders" at the expense of bona fide creditors. A subordinate clause in a provision obviously designed as a protection for other creditors ought not to "be given so extravagant an effect" (R. 152).

C. *The General Purpose of Section 77B.*

The general purpose of Section 77B was to provide a practical means of enabling embarrassed corporations to continue business in reorganized form. To this end, the definition of creditors is couched in broad terms and the statute provides, in subdivision (h), that the debtor and its assets shall be freed of all liabilities except such as may be specially reserved (*supra*, p. 5). To construe the statute as not providing for the reservation *in priority to stockholders* of any valid claims not presently allowable would, as we show below (p. 31), raise grave doubts as to its constitutionality. But the attainment of the dominant purpose of the statute—effective reorganization—requires that, so far as practicable, claims should be presently liquidated and allowed, rather than reserved. Therefore, it is not likely that Congress, which knew of the existence of the large lease obligations of many embarrassed corporations, intended that such obligations should be provided for by reservation rather than by present allowance.

III.

If the balance of the claim over three years' rent is not presently allowable the statute requires that the petitioners' rights under the covenant of indemnity be reserved in priority to stockholders, to the extent that their loss turns out to exceed the amount of the allowed claim.

Although the Special Master recommended the present allowance of the petitioners' claim only in an amount equal to three years' rent, his report made it clear that his action was without prejudice to the petitioners' contention that they were entitled to some further recognition in the proceedings in priority to stockholders, either by the subordinate allowance of the balance of their claim or by a reservation of rights (*supra*, p. 7).

Even if the Court of Appeals were correct in holding that the balance of the claim over three years' rent was not presently allowable, that would not require or even support the conclusion, to which the court passed without discussion, that the petitioners' rights were intended to be extinguished for the benefit of stockholders. The limitation provision at the very most relates only to the *allowance* of *claims*. Other provisions of the statute (*supra*, p. 5) recognize that in some instances *liabilities* must be *reserved* in the plan or the order confirming the plan or in the final decree.*

Where the rights to be reserved are subordinate to the rights of creditors whose claims are presently

* In this way the same effect is accomplished in reorganization proceedings as is accomplished in ordinary bankruptcy proceedings by the restriction of the bankrupt's discharge to provable debts.

liquidated and allowed, machinery can be devised for protecting the prior position of such creditors or for valuing the participation in the reorganization which is accorded to the debtor's stockholders and subjecting to the reserved rights only the value of that participation.* (Of course, it may be agreed between the creditors and stockholders, as one of the terms of reorganization, that such rights be reserved generally against the reorganized company.)

Therefore, even if the statute expressly provided, as it does not, that a landlord's claim should not be allowed in an amount in excess of three years' rent, or even that the claim should not be allowed at all, it still would not require or permit the discharge of the debtor and its assets from its contract obligations to the landlord *for the benefit of stockholders.*

If the entire claim is not presently allowable, the alternative interpretation which we are now suggesting is required in order to avoid raising grave doubts as to the constitutionality of the statute (*Interstate Commerce Comm.* v. *Oregon-Washington R. & Nav. Co.*, 288 U. S. 14; *Linder* v. *United States*, 268 U. S. 5) and to avoid the harsh and arbitrary inequalities produced by a contrary interpretation** (*Knowlton* v. *Moore*, 178 U. S. 41, 76-77; *United States* v. *Kirby*, 7 Wall. 482, 486).

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* Adequate machinery was devised to meet such a situation in *In re Mechanics Trust Company, supra.*

** See *infra*, page 39.

IV.

The limitation provision as interpreted by the Court of Appeals is unconstitutional.

Congress was without power to deprive the petitioners of their fundamental rights as creditors, *for the benefit of stockholders.* The bankruptcy clause of the Constitution authorizes no such legislative repeal of fundamental law and, even if within the general scope of the bankruptcy power, the attempted exercise of the power falls under the prohibition of the Fifth Amendment.

The Court of Appeals failed to understand the ground of the petitioners' attack on the constitutionality of the statute, saying that the petitioners' position "presupposes that the appraisal of the future value of real estate is so reliable a basis * * * that Congress was obliged to treat it as good against shareholders" (R. 153).

The petitioners do not urge that the statute is unconstitutional if not requiring the present allowance of their entire claim measured by the formula adopted or by any other formula. (As we have shown, the court itself, and not Congress, selected the formula to be used.) The petitioners recognize that Congress has the power in providing an effective bankruptcy system to exclude contingent claims from liquidation and present allowance, so long as such claims are not extinguished.

Our position is that, if the petitioners' claim is not presently allowable in excess of three years' rent, then the failure of the statute as interpreted below to preserve as against stockholders the petitioners' contract right to indemnity, to the extent that their loss turns out to exceed three years' rent, renders

the statute unconstitutional. The petitioners' complaint is that in reorganization proceedings their contract rights have been partially appropriated for the benefit of their debtor's stockholders by "legislative fiat". They complain that what has been offered them in return, which the Court of Appeals called a "truncated substitute" measured by a "pie-powder standard", is arbitrary and discriminatory.*

A. *The Bankruptcy Clause.*

There was nothing in the practical situation with which Congress was dealing in the enactment of Section 77B (see *Duparquet etc. Co.* v. *Evans*, 297 U. S. 216) which required the legislative repeal of the fundamental principle that the priority of creditors (however contingent their claims may be) over stockholders could not be evaded by any form of corporate reorganization (*Northern Pacific Ry. Co.* v. *Boyd, supra; Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.*, 271 U. S. 445; *Howard* v. *Maxwell Motor Co., Inc., supra*).

Even if the inherent nature of claims justifies their partial exclusion from present allowability *on a parity with other debts,* that does not necessitate the extinguishment of the unallowable portion of the claims *for the benefit of stockholders.* Contingent claims may be allowed or reserved in subordination to other debts but in priority to the interests of stockholders (*Block* v. *Bell Furniture Co., supra*), and corporations may be reorganized effectively without according

* Judge Learned Hand's description was quite apt. The decision below certainly "mutilated" and "lopped off" the petitioners' rights. If Congress intended to prescribe such a remedy, it well may be said that it had assumed the role of a medieval squire settling disputes at country fairs according to his own ideas of rough justice.

stockholders a participation at the expense of a single class of creditors.

The limitation provision as interpreted below is not reasonably adapted to the object in view—effective reorganization. As we have shown, it does not provide a ready method for the liquidation of landlords' claims, but requires a judicial determination of the total claim before the limitation, whatever may be its effect, may be applied. No time, trouble or expense is saved in the judicial determination of the total amount of landlords' claims; in fact, the application of the arbitrary yardstick merely adds a further operation to the task of liquidation. If by "effective reorganization" is meant a readjustment fairly preserving the relative positions of creditors and stockholders, the arbitrary limitation of the claims of certain creditors defeats the end in view.

In the Court of Appeals, the trustee urged that the instant case is ruled by the decision of this Court in *Norman* v. *Baltimore and Ohio R. Co.*, 294 U. S. 240. That argument, if followed to its logical conclusion, would lead necessarily to the establishment of the proposition that in the exercise of the bankruptcy power Congress may destroy ordinary contract rights against a solvent corporation for the benefit of its stockholders, without any compensation whatever. But it cannot be said that covenants contained in leases entered into by an ordinary business corporation, obligating it in certain events to pay damages or to indemnify its landlords against loss of rents, were afflicted with a "congenital infirmity" (294 U. S. at p. 304) which would have permitted Congress to abrogate them entirely for the benefit of the corporation's stockholders when it thereafter voluntarily sought reorganization. There is nothing in the lan-

guage of the statute or in the Committee reports or the debates which evidences a determination by Congress that even the partial destruction of such covenants *for the benefit of stockholders* was necessary to the effective reorganization of corporate tenants.*

As to the petitioners, the statute has been given a retroactive effect. There is not a mere incidental impairment resulting from the exercise of an admitted power; there is a direct taking, *pro tanto,* of all remedies and therefore of the contract itself (*Lynch* v. *United States,* 292 U. S. 571; *Gibbes* v. *Zimmerman,* 290 U. S. 326). It is no answer to say that no cause of action had accrued to the petitioners under their contract of indemnity, since their loss could not be ascertained until the end of the term. No cause of action had accrued to the creditor for the enforcement of the liability of a state bank's stockholders, in *Gibbes* v. *Zimmerman.* Yet this Court, while holding that the creditor had no property, in the constitutional sense, in any particular form of remedy for enforcing the stockholders' liability, spoke of his "substantial right to redress by some effective procedure" as guaranteed by the Fourteenth Amendment, thus recognizing such right as property. See, also, *Pierce* v. *United States, supra.*

Although the petitioners had no title or lien with respect to any specific property of the debtor at the time of the enactment of Section 77B, they had definite, specific rights with respect to *all the property of the debtor,* to the exclusion of the debtors' stockholders. The debtor was in bankruptcy. Its surplus assets remaining after the satisfaction of its

* No such limitation on landlords' claims was attempted in the enactment of the provisions for the relief of individual debtors (Sec. 74), or of railroad corporations (Sec. 77), or of municipal corporations (Sec. 80).

provable debts constituted a trust fund, none of which could have been distributed to stockholders to the prejudice of the petitioners. If the debtor had been wound up under the statutes of New Jersey (the state of its incorporation), the petitioners' rights against the surplus assets would have been protected fully either by the present allowance of their claim or by the impounding of the assets until the petitioners' actual loss could be ascertained (*Block* v. *Bell Furniture Co., supra; cf. Pierce* v. *United States, supra*). If the debtor had been reorganized through the machinery of a bankruptcy sale, any interest accorded to the stockholders on such reorganization likewise would have constituted a trust fund for the protection of the petitioners' rights (*Northern Pacific Ry. Co.* v. *Boyd, supra; Howard* v. *Maxwell Motor Co., Inc., supra*). The petitioners' right to priority over stockholders with respect to any disposition of the debtor's estate, and their pre-existing remedies for the enforcement of that right, are as fully entitled to constitutional protection as were the rights and remedies in *Louisville Land Bank* v. *Radford*, 295 U. S. 555.

Even if it could be said that some reasonable and ratable limitation of contingent, unliquidated claims for the benefit of stockholders is necessary or reasonably adapted to effective reorganization (which we deny), that would not advance the argument in support of the decision below. The arbitrary and unequal operation of the limitation on landlords' claims as interpreted below is discussed fully at pages 39-44, *infra*.

There is no relation whatever—certainly no reasonable relation—between the amount of three years' rent agreed to in a lease entered into many years ago and the present value of an agreement to indemnify

against loss of rents during a term which, as in the case at bar, has fourteen years to run. The only ground on which the Court of Appeals thought the limitation to three years' rent had a "rational relation to the end to be achieved" was that it ordinarily would permit a landlord to prove his losses for "four or five years" which, in view of the supposed difficulty of determining the "future value" of real property, the Court thought was "a period which Congress *might* well fix as the maximum forecast which it would be safe to act on" (R. 154). To this assumption there are several answers: (1) the limitation provision does not restrict landlords' losses or the liquidation of landlords' claims to any particular period (*infra*, pp. 39-41); (2) the liquidation of landlords' claims does not involve forecasting *future* values of real property; it is the *present rental value* for the unexpired term which is involved (*supra*, p. 14); (3) other claims equally or more difficult of liquidation are allowable in full (*infra*, p. 44); and (4) if claims may not be liquidated properly, that is no reason for extinguishing them for the benefit of stockholders (*supra*, p. 29).

Moreover, the limitation provision applies to all landlords' claims, irrespective of whether or not they may be supposed to be difficult of liquidation. As to claims concededly not involving difficulties of liquidation,* the provision clearly is beyond the bank-

* Landlords' claims may arise under covenants providing for the payment of liquidated damages measured by the formula which the Court of Appeals adopted for the liquidation of the petitioners' claim. Other claims concededly not involving any difficulty of liquidation may arise; *e. g.*, where a landlord had erected a building especially for the tenant's use or had paid a bonus to cancel a prior lease in order to give possession to the tenant, and a covenant had been inserted in the lease requiring the tenant, in the event of early termination, to pay the landlord as liquidated damages an amount equal to the unamortized portion of the landlord's expense.

ruptcy power, and since in this respect the provision is single and indivisible it cannot be upheld as to the petitioners' claim, even if it would be valid had it been restricted to claims of that character (*Illinois Central R. R. Co.* v. *McKendree*, 203 U. S. 514, 528; *The Employers' Liability Cases*, 207 U. S. 463, 496-501, 504).

Although we concede that the scope of the bankruptcy power has never been delimited by decision of this Court, it may be helpful to point out the novelty of the provision under discussion and its radical departure from anything heretofore attempted.

In *Louisville Land Bank* v. *Radford, supra*, this Court said of the Frazier-Lemke Act that no bankruptcy act had ever before undertaken to supply the bankrupt capital with which to engage in business in the future. That remark is fully applicable to a provision which transfers to a corporation's stockholders an interest of substantial value constituting a trust fund for a certain class of its creditors.

Nor has any bankruptcy act ever before attempted to discharge the debtor from liability on any claim not fully provable and entitled to share in the distribution of assets, the privilege of provability and the privilege of discharge always having been deemed, from the earliest times, "co-extensive and commensurate, and very equitable" (*Ex parte Groome*, 1 Atkins 115, 119). Moreover, discharge affects only the subsequent property acquisitions of the bankrupt, freeing him from "encumbrance on future exertion"; it does not free his existing assets (*Hanover National Bank* v. *Moyses*, 186 U. S. 181, 188, 192).

The provisions of bankruptcy acts authorizing compositions are not analogous. A composition can be

effected only with the consent of the class of creditors affected thereby and if judicially determined to be for the best interest of such creditors, after notice and opportunity to be heard. The limitation of landlords' claims applies inexorably, even over the protest of every landlord creditor, irrespective of the special facts and circumstances of the particular case and without any power in the court to determine or even consider its fairness (*cf. W. B. Worthen Co.* v. *Thomas,* 292 U. S. 426, 431; *National Surety Co.* v. *Coriell,* 289 U. S. 426; *First Nat. Bank* v. *Fleishem,* 290 U. S. 504, 525).

The arbitrary limitation of landlords' claims cannot be justified by reference to the power of Congress to recognize exemptions designed to afford some reasonable measure of relief to *individual* bankrupts. It is a benefit conferred on the stockholders of business corporations, which, unlike the usual exemptions, is not contributed *pro rata* by all creditors or even by all creditors with contingent, unliquidated claims, but is exacted entirely from one class of creditors arbitrarily selected under an inexorable rule (*infra,* p. 44). "The exemption * * * is unlimited. * * * There is no restriction with respect to particular circumstances or relations" (*W. B. Worthen Co.* v. *Thomas, supra,* at p. 431.) Moreover, retroactive exemptions are invalid (*Gunn* v. *Barry,* 82 U. S. 610; *Edwards* v. *Kearzey,* 96 U. S. 595; *In re Dillard,* Fed. Cas. No. 3912).

B. *The Due Process Clause.*

The bankruptcy power is subject to the limitations of the Fifth Amendment (*Louisville Land Bank* v. *Radford,* 295 U. S. 555, 589).

Even if the limitation of landlords' claims *for the benefit of stockholders* were within the general scope of the bankruptcy power—which we deny—the limitation here attempted, as interpreted below, is invalid. It is a "legislative decree", and is arbitrary and discriminatory.

(1) *The limitation provision is arbitrary and discriminatory.*

The inequalities and arbitrary discrimination produced by the statute are not incidental, occasional or only remotely possible, but are deliberate, "inevitable and profound" (*Knowlton* v. *Moore, supra*).

As to claims based on leases containing covenants to indemnify against loss of rent: If the proper formula for evaluating such claims is the difference between rent reserved and rental value, as we contend and as was held below, the three factors which enter into the equation are (1) the annual rent reserved; (2) the length of the unexpired term; (3) the present rental value for the unexpired term. The limitation provision takes the first factor, multiplies it by three, a figure selected out of the blue, and prescribes that the arbitrary result thus achieved shall measure the extent of the landlords' rights if it is less than his total claim, but shall be disregarded if it is in excess of his total claim. This arbitrary yardstick is applied after the landlord's entire claim has been judicially determined by the correct application of all relevant factors.

It is only theoretically possible—and then only by purest accident—that the provision can operate

equally as among landlords similarly situated. As the table printed on the opposite page shows, the provision may—almost must—operate unequally between two landlords even where the amounts of annual rent reserved are identical (Cases A and B; C and D); even where the unexpired terms of the leases are identical (A, B and C; E and F); even where the present rental values of the unexpired terms are identical (B and C; D and E); and even where any two of these three factors are identical (A and B; B and C); or where the total damages (D, E and F), or the respective ratios of total damage to total rent reserved (C, D and E), are identical.

In every case, irrespective of the identity of all other factors, the determining factor is three times the amount of the annual rent which happens to have been agreed upon when the lease was made, perhaps many years ago. Under that standard, one landlord's losses may be allowed for five years while the losses of another are allowed for twenty years. A more arbitrary, unrelated standard scarcely could be imagined. It necessarily produces wholesale inequalities.* Such inequality may not be sustained

* It has been said that the longer the unexpired term, the less chance there is of the landlord ultimately sustaining loss. This is specious; it ignores the fact that the landlord is not required or even permitted to speculate as to the future trend of rental values for the account or at the risk of the tenant. He is entitled and even required to replace his bargain as quickly as that can be done, by re-letting the premises for the entire balance of the term. If he has been unable to do so, opinion evidence as to the price which could have been obtained on such a re-letting must be resorted to. If he could have re-let for the balance of the term and failed or refused to do so, he nevertheless is chargeable with the amount obtainable, in computing his claim (*supra*, p. 14, footnote).

Aside from these considerations, the limitation provision does not discriminate only against landlords where the unexpired terms of their leases are long. It may also discriminate against landlords whose leases are short in favor of others whose leases are long (Cases A, D and F).

	A		B		C		D		E		F	
Unexpired term	10 yrs.		10 yrs.		10 yrs.		6 yrs.		4 yrs.		4 yrs.	
Annual rent	$10,000		$10,000		$12,000		$12,000		$18,000		$15,000	
Total rent reserved		$100,000		$100,000		$120,000		$72,000		$72,000		$60,000
Present rental value		70,000		40,000		40,000		24,000		24,000		12,000
Total damage		30,000		60,000		80,000		48,000		48,000		48,000
Allowable claim (3 yrs. rent)		30,000		30,000		36,000		36,000		48,000		45,000
Destroyed claim		none		30,000		44,000		12,000		none		3,000

(N. B. The above figures are regardless of discount. Substantially similar results would be obtained if the figures for *Total rent reserved* and *Present rental value* were adjusted at the same rate of discount.)

merely because "it is difficult to be just, and easy to be arbitrary" (*Stewart Dry Goods Co.* v. *Lewis*, 294 U. S. 550, 560).

The same unequal results follow even if the landlord's damage under a covenant to indemnify against loss of rents is considered to be, not the difference between rent reserved and rental value, but the actual loss as ascertained at the end of the term. The same unequal results follow as to claims for liquidated damages contracted to be computed by the formula applied in the case at bar. Entirely absurd results follow as to landlords' claims based on covenants to pay damages bearing no relation whatever to the amounts of rent reserved in the leases (see the footnote, p. 36, *supra*).

The Court of Appeals, although recognizing the gross inequalities produced by the statute as among different landlords, upheld the statute by a curious process of reasoning: the court thought (R. 154) that if Congress had limited landlords' claims to their *losses* for four or five years, *that would have been* reasonable, in view of the supposed unreliability of the formula used for measuring their losses; since ordinarily the limitation of claims to three years' rent would permit landlords to prove their losses for at least four or five years, the complaint against the statute is merely that when a landlord's "losses are large he is not treated equally with those whose losses are small". The court concluded that since "no lessor is unjustly treated as against his lessee, this is a complaint to which we are not disposed to lend an auspicious ear", because "nobody should be shocked that in a class of claims like these, so inherently uncertain, a piepowder standard is chosen, *even though it operates unevenly as unquestionably it does*". The court also suggested that only "the

lessee" could complain that some landlords might recover their losses for more than five years and that the lessee could not make this complaint because "he is getting a discharge upon a payment which he cannot show is too great until the occasion is past".

The Court of Appeals ignored the realities of the situation. It is inherent in any scheme of reorganization that every member of each class of creditors and stockholders should receive ratably equal treatment with his fellows in that class. But, under the statute as construed below, as we have shown, only by the merest accident can any two landlords receive treatment ratably proportionate to their losses, whether presently appraised or subsequently ascertained. That is a complaint, therefore, which should be available to any landlord who does not participate to the full extent of his actual loss.

Moreover, the remarks of the Court of Appeals are relevant only to a statute which Congress *might have enacted,* if it had desired to limit all landlords' losses to four or five years—not to the statute actually enacted (see *supra,* p. 16).

Finally, the view that "no lessor is unjustly treated as against his lessee" was based entirely on the assumption that a rough standard of justice must be applied because of the supposed difficulty of ascertaining the "future value" of real estate. To this there are two answers: first, it is a difficulty which affects only the question of whether the entire claim is *presently allowable* (*supra,* p. 29), and second, it is no difficulty even in that connection (*supra,* p. 14).

The statute produces other inequalities and arbitrary discriminations which the Court of Appeals ignored entirely.

The limitation is not applied to the claims of landlords of railroads, municipal corporations or individuals (Bankruptcy Act, Sections 77, 80 and 74). Although landlords' claims in ordinary bankruptcy proceedings were formerly not provable at all and now are provable only up to one year's rent, they were not formerly excluded and are not now limited for the benefit of the bankrupt or the stockholders of a bankrupt corporation.

The provision discriminates against landlords in favor of other creditors whose claims, although equally if not more difficult of liquidation, are not restricted for the benefit of stockholders.

Thus the discrimination against landlord creditors in Section 77B cannot be sustained as a valid classification based on the supposed difficulty of liquidating their claims.*

The arbitrary selection and wholesale discrimination attempted by the limitation provision as interpreted below bring it into conflict with the requirements of due process (*Heiner* v. *Donnan,* 285 U. S. 312, 331; *Nichols* v. *Coolidge,* 274 U. S. 531, 542; *Hoeper* v. *Tax Commission,* 284 U. S. 206; *Truax* v. *Corrigan,* 257 U. S. 312, 331).

(2) *The limitation provision deprives the petitioners of their rights by legislative decree.*

The provision operates automatically—without regard to the condition of the debtor, the extent of the

* It often has been urged that the landlord is a logical choice for discrimination, *because he gets his property back.* But the discharged employee is free to obtain new employment, and the holder of a forward contract for the sale of chattels has never even parted with his property;—yet these creditors participate in full. The landlord's claim, like their claims, is merely for the loss of his bargain.

stockholders' equity or any other particular circumstances of the case (*cf. Lowden* v. *Northwestern Nat. Bank & Trust Co.*, 298 U. S. 160). The judge has no discretion as to limiting landlords' claims. A landlord is not permitted to show that, under the circumstances, it would be unfair to limit his claim for the enrichment of the stockholders of a solvent corporation. On the question of whether the limitation is fair and equitable under the circumstances the landlord does not have a day in court or a hearing of any kind (*cf. National Surety Co.* v. *Coriell, supra*; *First Nat. Bank* v. *Flershem, supra*). "This is not legislation. It is a decree under legislative forms" (*Loan Ass'n* v. *Topeka*, 20 Wall. 655, 664). It is legislative usurpation of judicial power (*Louisville &c. Bank* v. *Radford, supra; Heiner* v. *Donnan, supra; cf. W. B. Worthen Co.* v. *Thomas*, 292 U. S. 426).*

If the limitation provision were intended as a short-cut method of liquidating landlords' claims, it still would be invalid. The determination of compensation for property taken and ordinarily the determination of damages are judicial functions (*Monongahela Navigation Co.* v. *United States*, 148 U. S. 312; *East Kingston* v. *Towle*, 48 N. H. 57). The admitted principle that where great difficulties inhere in the ascertainment of actual damages, the Legislature may provide, as to the future, for liquidated damages reasonably approximating the probable actual

* In *Louisville Land Bank* v. *Radford, supra*, the automatic extension of five years provided in the Frazier-Lemke Act was distinguished (pp. 596-598 of 295 U. S.) from the maximum extension of 2 years to be determined by the court, as provided in the Minnesota moratorium statute. In *Heiner* v. *Donnan, supra*, the legislative conclusive presumption that transfers within two years of death should be deemed to have been made in contemplation of death was held unconstitutional.

damages does not support the decision in the case at bar. The limitation on the claim of these petitioners is retroactive and the formula adopted bears no relation whatever, reasonable or otherwise, to the probable actual loss, whether that loss be estimated at the difference between rent reserved and rental value or its ascertainment be required to await the event.

It is clear, however, that the limitation provision does not purport to provide for liquidated damages. As we have shown, it does not assure every injured landlord of a claim equal to three years' rent, nor was it intended to assist in the ascertainment of any landlord's claim or injury. As interpreted below, the provision is and was intended to be merely a "truncated substitute", viz., a lopping off of all but a predetermined portion of claims already liquidated (and intended to be liquidated) by judicial process. We have found only one precedent for such an attempt. An early Pennsylvania statute undertook to limit certain claims for damages for personal injuries to the sum of $3,000. It was held to deny the right to a "remedy by due course of law" guaranteed by the Pennsylvania constitution (*Kay* v. *Pa. R. R. Co.*, 65 Pa. St. 269; *Passenger Rwy. Co.* v. *Boudrou*, 92 Pa. St. 475).

V.

The petitioners are entitled to question the constitutionality of the limitation provision as interpreted below.

Various objections have been advanced to the petitioners' standing to attack the constitutionality of the limitation provision. These objections fall generally

under two heads: (1) as to whether the petitioners are or will be damaged by the operation of the provision, and (2) as to whether the petitioners have waived, or are estopped to assert, the unconstitutionality of the provision.

A. *The Limitation Provision, as Interpreted Below, Inflicts Legal Injury on the Petitioners.*

In its brief in opposition to the petition, the trustee urged that the petitioners cannot show at the present time that they are in immediate danger of direct injury, because it cannot be established until the end of the term whether the amount of three years' rent is equal to or less than their actual loss. No method is available for presently evaluating in dollars and cents the petitioners' contract right to indemnity, other than the formula adopted below and universally accepted. It already has been shown that, if that method be adhered to, three years' rent does not equal the petitioners' actual loss. But if the trustee's contention were sound, it necessarily would follow that the question of constitutionality could not be determined until the amount of the petitioners' actual loss could be established. Therefore, the order now being reviewed is clearly wrong, in that it has cut off the petitioners' rights prematurely without reserving to them a seasonable opportunity of asserting their constitutional rights.

In overruling the petitioners' contention that the limitation provision as interpreted below deprived them of property without due process of law, the Court of Appeals said (R. 156):

> "But before holding that the substitute was here inadequate we must look at the position in

which these lessors would have found themselves if there had been no reorganization."

The Court of Appeals then proceeded to speculate as to the practical value of the petitioners' rights against the debtor prior to the enactment of Section 77B, saying that, since the debtor was already in default and subject to dismemberment by its creditors, and the petitioners' claim was not yet suable, their rights against the debtor in the absence of reorganization would have been "no better than if it were out and out insolvent." This reasoning is similar to the argument which was advanced unsuccessfully in the *Boyd* case, that the assets involved in that reorganization were insufficient to pay the mortgage debts, leaving nothing of value for general creditors. In that case this Court said that the superior rights of creditors over stockholders "must be decided according to a fixed principle, not leaving the rights of the creditors to depend upon the balancing of evidence as to" the value of the property, and that if the value of the property justified the issuance of securities to the stockholders "the creditors were entitled to the benefit of that value, whether it was present or prospective, for dividends or only for purposes of control", since "in either event it was a right of property out of which the creditors were entitled to be paid before the stockholders could retain it for any purpose whatever" (228 U. S. at pp. 507-8).

There has been no finding that the debtor is insolvent nor has its insolvency even been alleged. There is no basis whatever in the record to support the assumption of the Court of Appeals that the amount of immediately enforceable liabilities was so great that the debtor's dismemberment would have resulted from their enforcement, leaving no surplus which

would have constituted a trust fund for contingent creditors such as the petitioners. The order of the District Court limiting the petitioners' rights to participate in the debtor's reorganization was entered in the absence of any determination of the total amount of claims and in the absence of any determination of the value of the assets, and the only theory on which it could have been entered at that time was that those facts were entirely irrelevant to the issue. In this respect, the order refused to follow the report of the Special Master who attempted to defer the determination of the petitioners' rights in excess of three years' rent until the time arrived for the classification of creditors and the adoption of a plan of reorganization.

The petitioners are asking only that their claim in excess of three years' rent be allowed in priority to whatever interest otherwise might be available for stockholders, or that the order cutting down their claim to three years' rent be without prejudice as against stockholders. That is their fundamental right and they are not required to prove its value in dollars and cents in order to prevent being deprived of it. However, the insistence of the Preferred Stockholders' Protective Committee on the limitation of the petitioners' rights solely for the benefit of stockholders, as shown by the record, justifies the inference that the priority over stockholders for which we contend is not entirely without value.

B. *The Petitioners Have Not Waived, and Are Not Estopped to Assert, the Unconstitutionality of the Limitation Provision.*

In its brief in opposition to the petition, the trustee urged that the petitioners have no standing to chal-

lenge the constitutionality of the limitation provision because they "have accepted the benefit of the statutory scheme of liquidation". This means that the petitioners are estopped to question the partial destruction of their contract rights because they have demanded that they be allowed to prove, on a parity with provable debts, a claim in the amount of three years' rent, and because the courts below have upheld that position and the petitioners have not appealed.

The contention is wholly without merit. In their proof of claim, the petitioners followed the requirements of the statute as they understood it. It is true that they demanded that their entire claim be liquidated at the difference between rent reserved and rental value and that their claim be allowed on a parity with provable debts in an amount equal to three years' rent. But at the same time the petitioners also demanded that the balance of their claim be allowed in subordination to provable debts but in priority to the interests of stockholders (R. 4). Later, with the consent of all parties, the petitioners amended their proof of claim so as to demand that if any part of their claim should be held not provable their rights should, to that extent, be reserved against the debtor's assets, at least in priority to the interests of stockholders (R. 25).

Throughout the proceedings, the petitioners have asserted that the limitation provision is unconstitutional if interpreted as it was below.

The petitioners have as yet accepted nothing under the statute. The position which they have urged throughout the litigation has been upheld in part by the lower courts. There was no necessity on their part, nor had they any standing, to appeal from the order in so far as it was in their favor.

The preferred stockholders and the debenture-holders did appeal and urged in the Court of Appeals, as they had in the District Court, that the petitioners had no claim entitled to allowance in any amount. After their contentions were overruled by the Court of Appeals, they failed to apply for certiorari, and thus it may be that the question of the allowability of the three-year claim is not before this Court.* However, that is the result of the respondents' voluntary abandonment of their position below and cannot in any way prejudice the petitioners' rights in this Court.

If the respondents had brought the whole case to this Court, they might have been in a position to urge that the statute offered the petitioners an election either to prove a claim for three years' rent on a parity with provable debts, or to reserve in full their contract rights. If such a contention (which goes merely to the *interpretation* of the statute) had been made and upheld, the petitioners then would have been required to elect; up to the present time, they have made no election, nor have they been required to make one. Certainly the statute did not afford them the choice of either accepting its benefits or of failing to file a claim and later attacking its constitutionality.

Whatever might have been the result if the whole case had been brought to this Court, it is clear that in the existing situation the provision which the petitioners are entitled to receive under the decision below is only something to which they would be entitled in any event, irrespective of what interpretation may be placed on the limitation provision and irrespective of whether or not it is determined to be constitutional. There is no basis whatever for an estoppel.

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* The trustee has never questioned the petitioners' right to the three-year claim.

VI.

As to the relief to which the petitioners are entitled.

Ample evidence was adduced before the Special Master to enable him to determine the total amount of the claim, and he failed to do so only because he felt that all questions as to the petitioners' claim in excess of three years' rent should be reserved for future determination.

On this record, the order below should be reversed and

(a) the balance of the petitioners' claim over three years' rent, amounting to $43,314.75 (subject to discount), should be allowed in subordination to provable debts but in priority to the interests of stockholders;

or

(b) the disallowance of the balance of the petitioners' claim over three years' rent should be without prejudice to the right of the petitioners to demand appropriate reservation of their rights in priority to the debtor's stockholders, either in any plan of reorganization which may be confirmed by the District Court, or in the order confirming such plan, or in the final decree.

Respectfully submitted,

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(November 23, 1936.)

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 354

IN THE MATTER

of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor,

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,

Petitioners,

against

IRVING TRUST COMPANY, Trustee, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION ON BEHALF OF TRUSTEE

WILLIAM D. WHITNEY,
Counsel for Respondent,
Irving Trust Company, as Trustee.

DONALD C. SWATLAND,
R. L. GILPATRIC,
Of Counsel.

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OPINIONS BELOW

The opinion of the Special Master (Irwin Kurtz, Referee in Bankruptcy) appears on page 79 of the record and

is not reported. The opinion of the District Court (per Judge Knox) is found in the record at page 146 and is not reported. The opinion of the Circuit Court of Appeals (per Judge L. Hand) appears on page 150 of the record and has not yet been reported.

THE FACTS

In 1926 the petitioners' predecessors made a lease to the Debtor of property in the City of Trenton, New Jersey, for a term to expire on March 31, 1946 (R. 30, 46). The Debtor was adjudicated bankrupt on August 29, 1932, and its trustee in bankruptcy rejected the lease and surrendered the premises on November 14, 1932 (R. 5). Thereupon, the petitioners re-entered, terminated the lease and re-let[1] in pursuance of a clause in their lease by which the Debtor had covenanted that in such event it would

> "* * * indemnify the Landlords against all loss of rents which the Landlords may incur by reason of such termination, during the residue of the term above specified" (R. 58).

After Section 77B had been enacted and proceedings for reorganization of the Debtor begun, the petitioners filed a claim for the entire rent payable under their lease until its expiration in 1946, less the alleged fair rental value for the same period (R. 4-11). The Trustee conceded the allowability of a claim on the indemnity covenant, but moved to reduce it to an amount limited to the maximum of three years' rent plus accruals, as provided in the

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[1]Two-thirds of the premises were re-let until 1938 (part on a percentage basis) with the balance being occupied under monthly tenancies (R. 62, 70, 41).

statute (R. 15). The Trustee's position was sustained successively by the District Court and the Circuit Court of Appeals, and the claim allowed on such limited basis, *i. e.*, for $44,377.55 (R. 118).

QUESTIONS SOUGHT TO BE RAISED

This Court is asked to pass upon the construction and constitutionality of an act of Congress [Section 77B(b)(10)] which amended the Bankruptcy Act of 1898 to provide for the provability, to a limited extent, of landlords' claims for future rent in proceedings for reorganization of corporations. The questions are presented in respect of a lease containing an indemnity covenant, under which a claim has been allowed pursuant to such statutory provision but limited to a maximum of three years' rent as provided in the statute. The petitioners urge, *first*, that the statutory provision should not be construed as limiting their claim as against the interest of the Debtor's stockholders and, *second*, that if so construed the limitation provision is unconstitutional.

STATUTE INVOLVED

The provision of Section 77B (b) (10) of the Bankruptcy Act which is involved in this case reads as follows:

> "*The claim of a landlord* for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but *shall be limited*

to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *." [Italics ours.]

SUMMARY OF ARGUMENT IN OPPOSITION TO WRIT

(1) On the question of statutory construction we have nothing to add to the opinion of the Circuit Court of Appeals (R. 151). We refer this Court in addition only to the final conference report on the bill (H. R. 5884) subsequently enacted as Section 77B, an extract from which is set forth in an Appendix to this brief.

(2) As to the supposed unconstitutionality of the statute, the Trustee urges that a writ be denied to the petitioners for two reasons:

(a) The power of this Court to hold an act of Congress unconstitutional cannot properly be invoked in this case because the petitioners have not sustained, nor are they in immediate danger of sustaining, any direct injury as a result of the statute complained of.

(b) The decision below is manifestly correct, is in harmony with the applicable decisions of this Court and is not in conflict with the views expressed by any other circuit court of appeals.

ARGUMENT

POINT I.

THE CONSTITUTIONALITY OF THE PROVISION IN SECTION 77B LIMITING LANDLORDS' CLAIMS IS NOT RAISED BY THE APPLICATION OF THE LIMITATION TO THE PETITIONERS' CLAIM.

This Court has made it abundantly clear that its power to disregard Congressional enactments as unconstitutional will be sparingly exercised. *Massachusetts* v. *Mellon,* 262 U. S. 447, 488:

> "The party who invokes the power [to disregard an unconstitutional enactment] must be able to show not only that the statute is invalid but that he has sustained or is immediately in danger of sustaining some direct injury as a result of its enforcement, and not merely that he suffers in some indefinite way in common with people generally."

The claim here presented is based upon a covenant by the Debtor to indemnify the petitioners against loss of rent under their lease during the residue of the term ending in 1946. Such a covenant, this Court has twice held, does not give rise to a complete obligation until the expiration of the term, in this instance ten years hence, when the actual loss, for which the indemnity is provided, may be ascertained.[2] (*Manhattan Properties, Inc.* v. *Irving Trust Co.,*

---

[2]If rental values in the City of Trenton have appreciated by 1938 when the present re-letting arrangements run out, the petitioners may be able to obtain high enough rentals over the eight-year balance of the term to recoup their earlier losses. The property is unquestionably in a position to benefit from any improvement in real estate conditions (R. 31, 35).

291 U. S. 320, 338; *Miller* v. *Irving Trust Co.*, 296 U. S. 256, 258). In both cases cited, this Court flatly rejected the landlord's contention that an indemnity covenant of the type found in the petitioners' lease is the equivalent of an agreement by the tenant to pay liquidated damages in the event of bankruptcy.

Had the petitioners' lease contained a liquidated damages clause of the type held to give rise to a provable claim prior to Section 77B (*cf. Irving Trust Co.* v. *Perry Co.*, 293 U. S. 307), and had petitioners' damages under such clause exceeded the limit put by the statute upon landlords' claims, the petitioners might be in a position to raise the constitutional issue.[3] But such is not the present case, as the Court below recognized (R. 156).

The Court below, once having determined that a claim on the indemnity covenant was provable, did rule, to be sure, that the claim was "to be liquidated by discounting the future payments and subtracting the appraised value of the term from their sum" (R. 151). Whether that rule of damages was properly applied is not now at issue as this Court has not been requested to review the allowance of the claim in the amount of the statutory maximum. But in so ruling and in accepting what it recognized to be "speculative evidence of damages" (R. 153) the Court's interpretation of the statute as providing for the present liquidation of a future right was conditioned upon the effectiveness of the limitation. The petitioners have accepted the benefit of the statutory scheme of liquidation in the allowance of their claim for the statutory maximum upon an equality

[3]No claims have been filed by landlords of United Cigar Stores Company of America which raise any question of the applicability of the statutory limitation in cases where the leases contain liquidated damage clauses.

with other claims with which they were not entitled to share prior to Section 77B. They cannot look to the statute for the benefit and repudiate the limitation (*Calhoun* v. *Massie*, 253 U. S. 170; *Shepherd* v. *Mt. Vernon Trust Co.*, 269 N. Y. 234).

POINT II.

THE DECISION OF THE CIRCUIT COURT OF APPEALS UPHOLDING THE CONSTITUTIONALITY OF SECTION 77B (b) (10) AS APPLIED TO THE PETITIONERS' CLAIM PRESENTS NO QUESTIONS REQUIRING A REVIEW BY THIS COURT.

(a) The decision below is in accord with established principles and the applicable decisions of this Court.

In deciding that the provision in Section 77B limiting the petitioners' claim to three-years' rental was valid, the Court below necessarily considered, *first*, whether the statute falls within one of the congressional powers, and *second*, whether it represents a reasonable exercise of that power (*Norman* v. *Baltimore & Ohio R. Co.*, 294 U. S. 240).

(1) It is settled that it is within the scope of the bankruptcy power for Congress to provide for an *equitable distribution* of the assets of the estate (*Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224, 227). Indeed, this Court has said, referring to the allowability of future rent claims under the Bankruptcy Act prior to its amendment in 1934:

> "The issue is not one of power, for plainly Congress may permit such claims or exclude them." (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 332.)

The fact, so stressed in the petition herein, that the bankruptcy power has not heretofore been exercised to limit claims of a certain class of creditors does not detract from the existence of the power. (See *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, 587):

> "But, the scope of the bankruptcy power conferred upon Congress is not necessarily limited to that which has been exercised".

Indeed, since the Constitution was adopted, there have been many extensions of the bankruptcy power which, although "fundamental and radically progressive" in nature, have been "judicially approved or accepted as falling within the power conferred by the bankruptcy clause of the Constitution" (*Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pac. Ry. Co.*, 294 U. S. 648, 671).

Nothing said by this Court in the *Radford* case requires a conclusion different from that reached by the Court below. In the *Radford* case, while holding that as against the Fifth Amendment Congress could not under the bankruptcy power take away a vested right in specific real estate (in that case mortgage rights), this Court was careful to point out that a contrary rule applied where only a personal obligation was concerned. In such a case Congress, being free of constitutional inhibition upon the impairment of contracts (*cf. Hanover National Bank* v. *Moyses*, 186 U. S. 181, 186), has the power to limit or discharge personal obligations (See 295 U. S., at p. 589).

(2) There remains the question whether the particular limitation prescribed by Congress for landlords' claims is arbitrary or capricious, or whether it furnishes an appropriate means to the legitimate end of providing for equitable distribution under the Bankruptcy Act.

This Court had held that landlords' claims were not provable under the Bankruptcy Act prior to its amendment in 1934 (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320). When Congress set out, therefore, to make equitable disposition of landlords' claims under Section 77B, its problem was to concede something to a class which had nothing before. But in determining upon the treatment to be accorded to landlords, Congress could not fail to take into account the inherently speculative and contingent character of claims for loss of future rents, as recognized by the long line of federal cases culminating in the *Manhattan Properties* decision.

Congress might have adopted the equity rule barring contingent claims beyond deficiencies accruing to the end of the period for filing claims. The alternative was to treat landlords' claims as allowable where the debtor remained liable under a covenant for damages or indemnity and where there was present evidence of some loss. This, the Court below has held, is what Congress had in mind in order to avoid leaving an indeterminate amount of contingent claims to be dealt with in the plan of reorganization. Then, to spare the courts the necessity of speculating as to the precise amount of loss which might ultimately be sustained by landlords with long term leases, Congress put a top limit on all such claims.

The reasonableness of the statutory limitation as applied to the petitioners' claim can scarcely be questioned. It is one thing to grant, as was done here, that based on the most reliable evidence presently available, the petitioners' loss over the term would not be less than $45,377.55, the maximum amount allowable under the statute. But it is something else for a court now to be required to find *as a fact*

that by March 31, 1946, the claimants' loss will be $87,692.30 (the alleged differential between the rent reserved and the rental value as now estimated), or, indeed, that it will even equal $45,377.55.

(b) No conflict exists among the several Circuit Courts of Appeals.

The unanimous decision of the three Circuit Judges sitting below is the only express holding to date with regard to the limitation of landlords' claims provided in Section 77B. Thus no conflict has arisen among the several circuit courts of appeals to move this Court to grant a review. Indeed, the constitutionality of the limitation seems to have been assumed by the Circuit Court of Appeals for the Fourth Circuit in *Campbell* v. *Alleghany Corporation*, 75 F. 2d 947, 951, cert. den. 296 U. S. 581. Moreover, the only text-writer who has dealt with the subject agrees that the treatment of landlords' claims in Section 77B "is reasonably calculated to deal with the problem" (*Gerdes on Corporate Reorganization* (ed. 1936), Vol. I, § 34, p. 130).

CONCLUSION

The petition for a writ of certiorari should, for the reasons stated above, be dismissed, with costs.

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APPENDIX

Extract from House Report 1821, 73d Congress, 2d Session, with respect H. R. 5884:

"Amendment No. 14: Under the House bill, executory contracts, including claims for future rent, are made provable claims for the purposes of this section. The Senate Amendment limited claims for future rent to an amount equal to the rent reserved by the lease for 1 year.

The amendment agreed to by conference makes any person injured by the rejection of an executory contract or unexpired lease of real estate a creditor for the purposes of this section. The claim of the landlord for injury resulting from loss of future rents is limited to an amount not to exceed the rent reserved by the lease for 3 years next succeeding the date of surrender of the premises or the date of re-entry of the landlord, whichever first occurs, plus unpaid rent accrued up to such date of surrender or re-entry of the landlord. * * *"

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Supreme Court of the United States

No. 354

CAROLINE R. KUEHNER AND FREDERICK G. FISCHER, as Trustees,

Petitioners,

against

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders' Protective Committee, *et al.*,

Respondents.

IRVING TRUST COMPANY, as Trustee of the estate of United Cigar Stores Company of America, Debtor,

Respondent.

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT TRUSTEE

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Supreme Court of the United States

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as Trustees,
Petitioners,

against

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders' Protective Committee, *et al.*,
Respondents.

IRVING TRUST COMPANY, as Trustee of the estate of United Cigar Stores Company of America, Debtor,
Respondent.

No. 354

ON WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF OF THE REORGANIZATION TRUSTEE

The Opinions of the Courts Below

The opinion of the Circuit Court of Appeals is reported in 85 F. [2d] 35; the memorandum opinion of the District Court is unreported, but appears at R. 146; and the report of the Special Master appears at R. 79.

Statement of the Case

This is a petition by landlords, who have been allowed a claim in proceedings under § 77B of the Bankruptcy Act

for $44,377.55, being an amount equal to three years' rent (plus accruals of unpaid rent)[1] from the date of the landlords' re-entry following the Debtor's bankruptcy in 1932.

The landlords appeal from that part of the order which limited their claim to three years' rent, and which rejected their contention that the balance is allowable in subordination to other provable claims but in priority to the interests of the stockholders of the Debtor (R. 122).

Questions Presented

The Reorganization Trustee, which commenced this proceeding by moving to have the claim limited to an amount equal to three years' rent, files this brief in support of the order below granting such motion. The questions considered in this brief are therefore

(a) whether by the three-year provision in Section 77B (b) of the Bankruptcy Act Congress intended to limit landlords' claims as against stockholders and not simply their parity status with other creditors;

(b) if so, whether such a statutory limitation is a constitutional exercise of the bankruptcy power of Congress.

Statement of Facts

In October, 1926, the petitioners' predecessors made a lease to the Debtor of a building and store property in the

[1]This refers to accruals up to the date of re-entry, from which date the three-year period runs. As these accruals were allowed in this case, and (in our judgment) properly so, no further reference to this feature will be made in this brief.

business center of the City of Trenton, New Jersey (R. 30-32). The term was to run until March 31, 1946, at a net annual rental of $10,500 for the first ten years and of $11,500 thereafter (R. 46-47). The Debtor was adjudicated bankrupt on August 29, 1932, and its Trustee in Bankruptcy rejected the lease and surrendered the premises on November 14, 1932 (R. 5-6). The petitioners promptly reentered, thus terminating the lease according to its provisions (R. 57-58), and thereafter relet portions of the property from month to month or for short terms to other tenants (R. 41).

The Debtor had covenanted in the lease that in case of such termination

> "it will indemnify the Landlords against all loss of rent which the Landlords may incur by reason of such termination, during the residue of the term above specified" (R. 58).

After § 77B had been enacted and these proceedings begun, the petitioners filed a claim for the entire rent payable under the lease until its expiration in 1946, less the alleged fair rental value for the same period (R. 4-11). The Trustee objected to the claim as filed and moved to reduce it to an amount limited as provided by the statute (R. 12-17). The District Court and the Circuit Court sustained the objection and allowed the claim on such limited basis, *i.e.* $44,377.55.[2]

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[2]This figure exceeds the amount claimed in respect of three years' rent and accruals ($43,074.19, R. 10), but, pursuant to the Special Master's report (R. 93), is accepted by the parties as the proper computation of the claim.

Statute Involved

The controversy calls for a construction of the following portion of § 77B(b) of the Bankruptcy Act dealing with landlords' claims:

> "*The claim of a landlord* for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but *shall be limited* to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *." [Italics ours.]

Summary of Argument

I. The statute is unambiguous in its limitation of landlords' claims to three years' rent.

II. Resort to legislative history only confirms that it was the purpose of Congress so to limit landlords' claims.

III. The suggestion that, upon submission of the Plan of Reorganization, there should be proceedings for allowance as against stockholders of landlords' claims in excess of three years' rental, would defeat the purpose of the Reorganization Statute.

IV. The statute comes within the scope of the bankruptcy power. *Louisville Joint Stock Bank* v. *Radford,* 295 U. S. 555.

V. The statute represents a reasonable exercise of the bankruptcy power. The problem being to provide for an equitable distribution of the assets of the estate (*Kothe* v. *R. C. Taylor Trust,* 280 U. S. 224, 227), Congress is not limited in its choice of means to adopting the common law method of computation of damages in similar cases. Reasonable bases are readily apparent to support the principle of a statutory maximum as a means of providing a fair settlement to contingent creditors.

ARGUMENT

POINT I.

THE STATUTE IS UNAMBIGUOUS IN ITS LIMITATION OF LANDLORDS' CLAIMS TO THREE YEARS' RENT.

In the absence of ambiguity, there is no room for statutory construction. *St. Louis & Iron Mountain Ry.* v. *Taylor,* 210 U. S. 281, 294, 295; *United States* v. *Hill,* 248 U. S. 420, 424; *Adams Express Company* v. *Kentucky,* 238 U. S. 190, 199.

This statute is "plain on its face", *Asiatic Petroleum Co.* v. *Insular Collector,* 297 U. S. 666. It first describes the claim and then says that the claim "SHALL BE LIMITED to" three years' rent. There is no condition, exception or limitation.

And there is no hint or suggestion that there is to be a distinction between the amount for which the claim shall be provable on a parity with § 63(a) claims, on the one hand, and an amount provable in subordination thereto but superior to the rights of stockholders, on the other hand. The provision is simply that "The claim" * * * "shall be treated as a claim ranking on a parity with debts which would be provable under § 63(a) of this act," but "shall be limited" to an amount equal to three years' rent, etc.

POINT II.

RESORT TO LEGISLATIVE HISTORY ONLY CONFIRMS THAT IT WAS THE PURPOSE OF CONGRESS SO TO LIMIT LANDLORDS' CLAIMS.

If it were proper to resort to legislative history as an aid to construction of a statute so plain on its face, that history (as described in the petitioners' brief) would itself be decisive and in our favor. It shows that the bill before Congress first provided for the very distinction (between parity claims and subordinated claims) contended for by the petitioners, and then that Congress deliberately obliterated the distinction by amendment (*Wood* v. *Broom*, 287 U. S. 1, 7-8). It even shows the compensation for the amendment, as the bill first provided only for one year's rent on a parity, and the balance subordinated (H. R. 5884; May 7, 1934, p. 11); whereas the amendment struck out the latter provision, and raised the former to three years (H. R. 1821; May 29, 1934, p. 2).

In other words, the bill first provided that such claims should be provable on a parity with §63 (a) claims, up to the same amount for which rent claims were by the same

statute[3] made provable under §63 (a) (viz., 1 year), and that the balance of the claim should be subordinated to provable claims but preferred over stockholders. But Congress evidently then determined that such provision would call for unduly complicated proceedings, out of harmony with the purpose of § 77B to obtain a summary and speedy reorganization. *Continental Illinois Nat. Bank & T. Co.* v. *Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648, 685. It turned, therefore, to a practical, yet equitable, disposition of the matter, by making the entire amount of such a claim provable *as* a claim, and subject to a maximum amount, which it then raised to three years' rent.

POINT III.

THE SUGGESTION THAT, UPON SUBMISSION OF THE PLAN OF REORGANIZATION, THERE SHOULD BE PROCEEDINGS FOR ALLOWANCE AS AGAINST STOCKHOLDERS OF LANDLORDS' CLAIMS IN EXCESS OF THREE YEARS' RENTAL, WOULD DEFEAT THE PURPOSE OF THE REORGANIZATION STATUTE.

The petitioners suggest that, if their interpretation of the statutory provision in respect of the excess of their claim over the amount of three years' rent be accepted, there must be a hearing and determination as to the treatment to be accorded such excess at the time of submission of a plan of reorganization. A similar suggestion was adopted by the Special Master (R. 88) and is now urged upon this Court by the brief *amicus curiae* filed on behalf

[3]Act of June 7, 1934, §4 (7), as amended June 18, 1934, amending §63 (a) of the Bankruptcy Act, 11 U. S. C. 103 (a) (7).

of Jacob Ruppert Realty Corporation, an intervenor in the reorganization proceedings of the Debtor.

Any such suggestion, if adopted, would, it seems to us, utterly defeat one of the prime purposes of Section 77B. Under that statute, an expeditious reorganization is the end to be attained. But, if the landlords' claims for future rent (and these constitute the great bulk of the litigated claims in this estate) are not to be fully determined until the time of hearings on the plan, confirmation of the plan may have to be deferred for a long period thereafter. This is because a landlord claimant or an objector would be entitled as of right to carry any question as to the treatment of the excess claim from the Special Master to the District Court, and in turn, to the Circuit Court of Appeals, and (as in the present case) might well be granted a review by this Court on writ of certiorari. The present case provides an example of the time-consuming effect of such a procedure, as it has been handled most expeditiously, and yet the argument in this Court will be nearly one year and a half after the initial hearing before the Special Master (R. 18).

And we can find no support in the statute for this theory. There is no distinction made anywhere in the statute between claims *allowable* for the purpose of fixing the rights of creditors, and claims *allowable* for the purpose of determining the interests of stockholders. The statutory scheme is to determine the relative rights and priorities of creditors and stockholders alike, in a single proceeding or set of proceedings, and then to base an appropriate plan of reorganization on the results of that determination.

We conclude, therefore, that the important question in the case is the constitutional one,—whether Congress has the power, as against the Fifth Amendment, to provide for allowability of contingent landlords' claims and then to impose a maximum limit on the amount for which they may be allowed.

POINT IV.

THE STATUTE COMES WITHIN THE SCOPE OF THE BANKRUPTCY POWER.

As this Court pointed out in *Louisville Joint Stock Land Bank* v. *Radford,* 295 U. S. 555, the historic purpose of bankruptcy legislation has been the discharge of personal obligations of the bankrupt.

The decision in the *Radford* case was evidently put upon the ground that, as against the Fifth Amendment, Congress could not, under the bankruptcy power, take away a vested right in specific real estate (in that case mortgage rights). This Court was careful to point out that the contrary rule applied where only a personal obligation was concerned, and that in such a case the Congress (being free of constitutional inhibition upon impairment of contracts) had the power to limit or destroy personal obligations. See the opinion, 295 U. S. at page 589:

> "Under the bankruptcy power Congress may discharge the debtor's personal obligation, because, unlike the States, it is not prohibited from impairing the obligation of contracts."

This distinction between secured debts (representing vested rights in specific property) and unsecured debts

(personal obligations), and consequently between the power of Congress (which may discharge the latter, but not the former) and the power of the states (which may discharge neither), has long been recognized. In the leading case of *Hanover National Bank* v. *Moyses,* 186 U. S. 181, 188, Mr. Chief Justice Fuller thus expressed the same distinction:

> "The subject of 'bankruptcies' includes the power to discharge the debtor from his contracts and legal liabilities, as well as to distribute his property. The grant to Congress involves the power to impair the obligation of contracts, and this the States were forbidden to do.
>
> "The laws passed on the subject must, however, be uniform throughout the United States, but that uniformity is geographical and not personal, and we do not think that the provision of the act of 1898 as to exemptions is incompatible with the rule."

Accord: *Stellwagen* v. *Clum,* 245 U. S. 605, 613: the test of uniformity is "geographical and not personal."

The statute here under consideration does not have for its purpose the abridgement of creditors' rights in specific property, but it deals solely with the discharge of the personal obligations of the Debtor. Thus, the statute comes clearly within the scope of previous bankruptcy acts and does not transcend the bankruptcy power of Congress.

POINT V.

THE STATUTE REPRESENTS A REASONABLE EXERCISE OF THE BANKRUPTCY POWER.

There is no conflict between the circuits on the constitutionality of the statutory limitation. As far as we

know, it has been considered only in the second and fourth circuits, viz., in this case and in the case of *Campbell* v. *Alleghany Corporation*, 75 F. [2d] 947, at page 951, cert. den. 296 U. S. 581. In the latter case, the constitutionality of the provision was assumed. It is our position that these decisions are consistent with the fundamental test applied by this Court in such cases, viz., the test whether a statute represents *a reasonable exercise* of one of the recognized Congressional powers.

(A).

Principles Applicable.

It is settled that it is within the scope of the bankruptcy power for the Congress to provide for an *equitable distribution* of the assets of the estate, *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224, 227.

Congress is not shorn of judgment in the matter, and left simply to the judicial task of reading and applying the respective State laws.[4] If that were the full scope and extent of the congressional power, the word "equitable" would be without meaning.

The suggestion by the petitioners in this case comes to this: That any effort by Congress itself to legislate as to the adjustment of claims is unconstitutional, the argument being that the Constitution requires each claim to be passed upon judicially, and with a single eye to the determination

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[4]Indeed, in so far as the issue is one of power alone, the determination of Congress may well be absolute, even to the point of excluding such claims altogether from the statutory scheme of distribution (*Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 332).

of the extent to which it would or would not be recoverable under State or common law.

A fallacy in the petitioners' argument is that it starts with the assumption that the landlord's "injury" under the statute is necessarily represented by the difference between (*i*) the rent reserved and (*ii*) present rental value, *i.e.*, the rent that would be agreed upon for the balance of the term if the landlord were forced to contract for the entire balance of the term at the time of the bankruptcy.

But when leases are terminated for default after bankruptcy, landlords are not necessarily compelled forthwith to contract for the entire balance of the term. It is common knowledge that bankruptcies of companies subject to leasehold obligations normally occur in times of depression when markets are demoralized and rents are low. It would be poor business for landlords with bankrupt tenants, particularly those having long term leases, to contract at such a time for the entire remaining term of the lease; and it would be a rigorous law that would require all creditors and stockholders to submit to an inflexible rule that the landlords' injuries are to be measured on that basis.

It is common knowledge that the future is unknown and that the speculative character of prophecy increases rapidly as the span of time becomes longer.

It is equally common knowledge that cycles of depression have been consistently followed by cycles of rising prices and values,—not least, of rental values. The petitioners' argument is, in its effect, that Congress must ignore this fact, of which all have knowledge; that it is beyond the constitutional power of Congress to take account of the prospect that periods of depressed values, carrying with them depressed rents and bankruptcies, will be succeeded by periods of rising values and rising rents.

The petitioners state that they base their argument on *Filene's Sons* v. *Weed,* 245 U. S. 597, and *Irving Trust Company* v. *Perry,* 293 U. S. 307, which recognized that, where two private parties had contracted that recovery should be measured by the difference between rent reserved and present rental value, the contract is fair.[5] They develop their argument just as they would have done if Congress had enacted a statute that all landlords' contracts should be liquidated in bankruptcy upon the same basis as the contracts considered in the *Filene* and *Perry* cases. But this was not the statute enacted.

And there is certainly no constitutional requirement that the statute that was enacted should be so construed. It is absurd to say, and unsound to assume, that when this Court has approved a contract as fair (*i.e.,* as not amounting to a penalty, compare *Kothe* v. *R. C. Taylor Trust,* 280 U. S. 224), thereafter Congress is precluded, when legislating on

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[5]Although the petitioners suggest that the formula which they advocate is the accepted, if not the required, method of judicially determining landlords' claims, many of the cases which they cite (or refer to as having been cited in the *Filene* case) for this proposition, do not support it. Some of the cases were not decided until after the term of the lease had expired or there had been a reletting for the balance of the term, so that there was no longer any uncertainty either as to the event or as to the amount of the loss sustained by the landlord, *McGraw* v. *Union Trust Co.,* 135 Mich. 109; *Smith* v. *Goodman,* 139 Ill. 75; *Woodman* v. *Wise,* 112 Md. 35; *People* v. *St. Nicholas Bank,* 151 N. Y. 592. In other of the cases the landlord was denied any recovery at all for future rent, *Ex parte Blake,* 11 Ch. Div. 572; *Woodbury* v. *Sparrell Print,* 197 Mass. 426; *International Trust Co.* v. *Weeks,* 203 U. S. 364; *Bowditch* v. *Raymond,* 146 Mass. 109. And in still others, while the courts did arbitrarily award the landlords flat sums as approximating the future deficiency, the exact method of computation is not disclosed, *Leo* v. *Pearce Stores Co.,* 54 F. (2d) 92, 57 F. (2d) 340; *In re Carruthers,* 15 Rep. 317; *In re Reading Iron Works,* 150 Pa. St. 369.

the same subject, from adopting any other fair provision. Indeed, there can be no question but that, once having recognized as fair the formula for computing damage in the *Filene* case, this Court would likewise have approved a further provision in such formula limiting the damage in any event to say three years' rental.

Moreover, in this case, the petitioners do not even have the type of contract that was present in the *Filene* and *Perry* cases. The provision therein considered (known as the "*ipso facto* clause") was one that has been used in leases looking to protection of the landlord in the event of his tenant's bankruptcy. But more familiar is the entirely different type of clause known as the "indemnity clause", of which the present lease provides an example (R. 58).[6]

The untenability of the petitioners' position is neatly shown by the following sentence in their brief (at p. 15):

> "Nor does the use of the formula [the *Perry* case formula] involve an attempt to forecast the amount of rent the Landlord will lose over the remainder of the term."

But the petitioners' claim is based upon a covenant that the tenant

> "will indemnify the Landlords against all loss of rent which the Landlords may incur by reason of such termination, during the residue of the term" (R. 58).

Therefore, the very thing that the formula, upon which the petitioners rely, does *not* attempt to accomplish, is the only thing to which the petitioners' covenant entitles them.

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[6]The two types of clause were recognized in the opinion in *Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 337-338.

The distinguishing characteristic of the *"ipso facto* clause" is that it first presumes, for the purpose of creating a formula for liquidating damages, that rental values at the time of bankruptcy will remain the same over the term of the lease, and then makes that presumption irrebuttable. Quite different is the "indemnity clause" which, instead of applying a formula based on a mere presumption, provides that the landlord shall have no more and no less than actual *indemnity* over the full term of the lease.

The one forecasts the loss over the long term and irrevocably assumes that future value will be the same as present value. The other refrains from making any forecast at all and awaits the end of the term in order that it may make an accurate determination based on actual experience, *Hermitage* v. *Levine,* 248 N. Y. 333.

Neither provision is perfect. The one is over-bold because it closes its eyes to the prospects of future changes (which over the period of a long term lease are certain to occur); the other is unduly timid, because it awaits certainty, and recognizing that a present forecast involves some element of speculation, refuses to make any forecasts at all.

And neither clause meets the peculiar problem of a reorganization proceeding. That calls for a speedy determination or liquidation of all claims. On the other hand, speed is not to be attained either by sacrificing contingent creditors to the other creditors or by sacrificing the other creditors to contingent creditors. Thus, individual holders of contingent claims are not to be ruthlessly eliminated (as was often done under the old bankruptcy practice), nor, on the other hand, are their claims to be hastily and negligently allowed at excessive levels.

The clause that Congress enacted was accordingly one which would provide compensation for the "injury" to the contingent, as well as to the ordinary, creditor, but which placed some limitation on the degree to which that "injury" could be speculatively forecast and measured.

Our problem is not, therefore, whether the Congressional provision is like the clause in the *Filene* lease, or like the "indemnity clause" in the present lease. It is like neither. Our problem is rather whether the Congressional provision is reasonable in itself, or is arbitrary and capricious.

Before passing to that question, we should point out that the Court is not called upon here to consider whether a claimant with an *"ipso facto* clause" (such as was present in the *Filene* and *Perry* cases) would be entitled to the full benefit of that clause or would be confined by the three year limitation. It may be that such a clause, because it gives rise immediately upon bankruptcy to an independent personal covenant apart from the real estate provisions of the lease, *cf. Irving Trust Co.* v. *Perry,* 293 U. S. 307, 311, would not be subject to the three year limitation. But the same thing is by no means true of the "indemnity clause".

Indeed it was argued below by the debenture holders' and preferred stockholders' committees that the effect of the "indemnity clause" is to deprive the landlord of any present recovery at all, and at the least to postpone him to a recovery against the reorganized company at the end of the term, when his claim would be allowable on common law principles. But a disposition of the latter character, although giving to the claimant landlord no less than his contract calls for, would be a serious handicap to any reorganization. With leases running (like this one) to 1946, others

running for 99 years, and others for terms of varying duration, the reorganized company would be assuming recurrent, but uncertain, commitments. It might be that rental values would rise sufficiently over the 14 year period or the 99 year period to immunize the reorganized company from any obligation on indemnity covenants. It might be that rents would so decline as to render those obligations absolutely crippling. It makes no difference which; the governing point is that either possibility clouds the future of the reorganized company with uncertainty.

The Congress therefore, in providing for a present recognition of claims of this character, was not recognizing an existing contractual right (as might be the case with a *Filene* or a *Perry* type claim), but was by statute giving to landlords a claim on which otherwise they might never realize, and on which they certainly could not realize for many years.

Petitioners' argument, in referring to the analogy of equity reorganizations (*cf. Northern Pacific Railroad Company* v. *Boyd,* 228 U. S. 482, and *Howard* v. *Maxwell Motor Company,* 269 Fed. 292, 275 Fed. 53), overlooks the fact that, under those cases, when read together with the rule in *Hermitage* v. *Levine,* 248 N. Y. 333, no claim would arise to the petitioners until 1946. Accordingly, the petitioners omit to mention that § 77B gives them a new remedy of substantial tangible value, in that it gives them an immediate claim in lieu of one that would otherwise have been deferred for 14 years and might then not exist at all.

But, if we are to assume for the purpose of the argument that *present* rental value must be accepted as the only practicable base of determination of *future* damages, *i.e.,* if we must reject the suggestion which has been inherent

in our argument to date (to wit, that testimony could well be taken as to future probabilities in rental value), still this method of approach remains necessarily uncertain, and the longer the future term, the greater the uncertainty.

The ultimate question is always as to what the loss will be in the future. That is the real "injury". But that cannot be scientifically answered by determining what the loss would be only on the present basis.

However, if prophecies as to the future are, on practical grounds, to be eliminated from evidence, and only the present may be testified to, then it is obviously not improper to provide for an adjustment or correction of the present valuation so as to discount (as it were) changes probable in the future. If it is probable that the future values will exceed present values, then present estimates should be reduced. If it is probable that the future values shall be less than the present values, then present estimates should be increased.

As we have pointed out, the normal situation in the case of a tenant's bankruptcy is that it occurs during a period of depression, and consequently when it is probable that rentals in the future will increase. Accordingly, Congress takes an appropriate method of correcting the present estimate to adjust for future probability, when it places a maximum limitation upon the present estimate of loss.

We now revert to the question whether, taking all of these factors into consideration, Congress was constitutionally entitled, when it determined to permit such claims to be allowed, to place a maximum upon the amount for which they might be allowed.

Judicial decisions on the subject of the application of the bankruptcy law to leases prior to the adoption of § 77B

recognized the two elements of uncertainty,—uncertainty as to whether there would be any loss at all, and uncertainty as to the amount of that loss (if any). See *Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 331; *In re Metropolitan Chain Stores* (*First National Bank* v. *Irving Trust Co.*), 66 F. [2d] 485, 487 (C. C. A. 2); *cf. Wolf* v. *Stix*, 99 U. S. 1, 8.

The petitioners argue that Congress may constitutionally legislate on the subject of the first contingency, but not of the second. They say that Congress may provide for a future loss, notwithstanding that the courts have long recognized that it is uncertain whether there will be any loss, but that Congress may not provide for some recognition of the uncertainty as to the amount of such loss, notwithstanding that the courts have long recognized that uncertainty also. The argument places the courts in this paradoxical position,—that, notwithstanding that they themselves have heretofore been free to recognize both uncertainties, they are now asked to prohibit to Congress the right to recognize either.

But, it is suggested, the limitation here placed by Congress on the amount of provable future loss is arbitrary, because it is based on a fixed number of years of full rent. An elaborate table is submitted (petitioners' brief, p. 41) to indicate that an allowance *equal to* three years' rent would have a different practical effect in different cases. But this is without significance, for the three years is not to be the amount provable but is to be the *maximum* amount provable. Congress did not say that the various hypothetical landlords, imagined in the petitioners' brief, *should* each receive the equivalent of three years' rent. Some might receive the equivalent of two years' rent, some of one, some of six months, some of three months, and an

occasional one might receive, as do the petitioners, the equivalent of three full years' rent. But certainly all are not to receive the maximum.[7]

In seeking the Congressional intention, as we are now doing, the established rule is that we must recognize its constitutional validity if there be any reasonable ground to support it.

What then are the reasonable grounds upon which Congress may have acted?

First and foremost, Congress doubtless took account of what is really a certainty, viz, that the future is unpredictable. As expressed by Judge Learned Hand for the Circuit Court of Appeals

> "The appraisal of realty at a distant time is the merest guess; nobody can possibly know anything about it, and one man's guess is nearly as good as another's. For this reason Congress might circumscribe its use to the near future, not only as against creditors, but as against the lessee itself." (R. 153.)

Further reasonable grounds for the Congressional view are easily discernible. Congress may have felt that 50% was a reasonable maximum recognizable decline in rents during a depression, and that six years was a reasonable maximum period of time to forecast the continuance of a depression. Or it may have felt that 75% was a reasonable maximum recognizable decline in rents during a depression,

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[7]But, it may be said, if Congress could impose a maximum, should it not also be required to impose a minimum (as, that all landlords' claims shall be allowed for at least one year's rent)? The answer is obvious: that a landlord may, for example, have relet for the full or a higher rental to a fully solvent tenant.

and that four years was a reasonable maximum period of time to forecast the continuance of a depression. Either forecast would lead to the provision as enacted.

Each forecast, and others of the same character that may be imagined, would be based on the twin principles already enumerated, *first,* that landlords will probably lose something, *second,* that they will probably not lose over a long-term lease as much as they would lose if rental values were to remain at depression levels.

The principle of a statutory maximum[8] is, therefore, in fact based on the forecast that depressions will end and values will rise. But (it may be said) this is not certain. We agree; yet Congress is not confined in its reasoning to reliance upon certainties. It may weigh possibilities, and certainly may base its legislation upon probabilities.

What then is the extent of the probability of which Congress has taken account? It is a probability of the strongest character in the field of economics, in that it is a probability which will become a certainty *unless* the whole course of our economic history be reversed, as must be the case if the series of economic cycles be replaced by permanently low levels.

But surely neither the landlord nor any other citizen has a constitutionally vested right in an assumption that depressions will be permanent.

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[8]The principle of legislative fixing of maximum periods of time is, of course, well-established in the Bankruptcy Act, e. g. the four months' limitation for setting aside preferences, and the six months' limitation for proving claims. Each of these provisions is binding, notwithstanding that the mere chance of an event's falling within a rigidly predetermined period of time may cut off entirely a claimant's right in a given case.

(B)

APPLICABLE AUTHORITIES IN THIS COURT AND THE LOWER FEDERAL COURTS.

This Court has firmly established the principle under which the broad powers of Congress can be respected and enforced, without running to arbitrary or absurd results.

So here, the Congress has made a decision that three years' rental provides a reasonable maximum degree of limitation on the provability of this inherently contingent and speculative type of claim. That decision is not arbitrary or capricious. It is not devoid of a reasonable relationship to the legitimate end of providing for equitable distribution under the Bankruptcy Act (*Kothe* v. *R. C. Taylor Trust,* 280 U. S. 224, 227). On the contrary, it represents an effort to make a reasonable appraisal of that factor of uncertainty which, according to the earlier decisions under the Bankruptcy Act, had appeared to the courts to be of absolutely decisive importance against Landlords' claims.

Heiner v. *Donnan,* 285 U. S. 312, relied on by the petitioners, is an example of the invalidation of a statute because "arbitrary and capricious". The last words appear repeatedly in the opinion, 285 U. S. at pp. 326, 330, 332. The holding of the Court was that a tax statute was invalid which attempted to establish an irrebuttable presumption that a gift within two years of death was made in contemplation of death. The Court's view is illustrated by the following, 285 U. S. at p. 327:

> "The presumption here excludes consideration of every fact and circumstance tending to show the

> real motive of the donor. The young man in abounding health, bereft of life by a stroke of lightning within two years after making a gift, is conclusively presumed to have acted under the inducement of the thought of death, equally with the old and ailing who already stands in the shadow of the inevitable end. * * *"

The mere determination of the amount of time prior to death could in *itself* have no possible relation to the question as to the intent of the donor at the time.

The problem of Congress under §77B was to make an equitable disposition of landlords' claims not previously provable. This Court had called attention to the fact that as a practical matter the landlord was wiped out under the existing law; it had recognized (in the *Manhattan Properties* case, 291 U. S. at pp. 331-332) the landlords' argument of

> "unfairness to the landlord of a corporate bankrupt who, under the decision below, cannot prove upon his lease along with other creditors, but must look solely for redress for loss of future rents to a corporate debtor whom bankruptcy has stripped of all assets."

The problem of Congress was, therefore, to award something to him who had nothing before.

In determining upon such treatment for landlords as a a class, Congress could not fail to take into account the inherently speculative and contingent character of claims for loss of future rents, as recognized by the long line of federal cases denying provability to such claims under Section 63a of the Bankruptcy Act prior to its amendment in 1934. *Manhattan Properties, Inc.* v. *Irving Trust Co.*, 291 U. S. 320, 335. To allow proof beyond the three-year

maximum would thrust the determination of damages far beyond the bounds of normal forecasting of real estate value and into the realms of conjecture and guess-work. It was this consideration that was uppermost in the mind of the District Judge, when he referred to the limitation as being "intended to put at rest the interminable speculative considerations that had to be taken into account in arriving at damages growing out of broken leases" (R. 146).[9]

Congress may also have had in mind the vital difference in substance between landlords, on the one hand, and most other classes of creditors, on the other. The landlords get their properties back, together with the right to all future appreciation in value over what may be a long term; yet they seek damages in addition. The merchandise creditor and the bondholder normally present the largest class of other creditors. They have parted with their property or money, as the case may be, and get nothing back but their claim.[10]

The claimants argue that *Northern Pacific Ry. Co.* v. *Boyd,* 228 U. S. 482, and similar cases (such as *Howard*

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[9]Would it not require the gift of prophecy to foresee that rental losses would exceed 50% over six years or 25% over twelve? See *Leo* v. *Pearce Stores Co.,* (D. Mich.) 57 F. [2d] 340, for a review of an actual trial of such a case. See also Judge Patterson's opinion in *In re Wise Shoes, Inc.,* 2 Fed. Supp. 521, aff'd *per curiam* (C. C. A. 2) 64 F. [2d] 1023.

[10]These considerations have previously been submitted to this Court (to quote from p. 332 of the opinion in the *Manhattan Properties* case):

> "The respondent asserts a substantial difference between rent and other kinds of indebtedness, and presents equitable considerations thought to weigh in its favor * * *."

v. *Maxwell Motor Co.* in the Second Circuit, 269 Fed. 292, 275 Fed. 53), compel a conclusion in their favor. It was there held that a court of chancery would not permit stockholders to share in a reorganization which did not make fair provision for any class of creditors, and that a creditor for whom such provision had not been made in the plan could follow the assets in the hands of the purchaser at the foreclosure sale. In applying this "fixed principle" referred to in the *Boyd* case this Court has encouraged "reasonable" and "practical" adjustments of the several rights of creditors and stockholders "measured by the existing circumstances" (See *Kansas City Terminal Railway* v. *Central Union Trust Co.*, 271 U. S. 445, 455).

While the chancery cases are without binding effect as to the power of Congress, they do indicate the Courts' opinion of what is or is not fair in dealing with this kind of problem. As in the case of equity reorganizations, the prime purpose of § 77B is to provide a basis, fair to creditors and stockholders alike, for continuing the enterprise without dismemberment or liquidation. Indeed, the acceleration of the claim of a holder of an "indemnity clause", accompanied by the three-year limitation, may well be said to constitute on the part of Congress a "fair offer" to creditors within the meaning of the decisions of this Court on the subject of equity reorganizations. *Cf. Kansas City Terminal Railway* v. *Central Union Trust Co.*, 271 U. S. 445, 454.

But, however that may be, "when a statutory system is administered, the only question for the Courts is what the statute prescribes", *Wm. Filene's Sons Co.* v. *Weed*, 245 U. S. 597, unless the statute is clearly unfair, arbitrary or capricious.

Legislative limitation of amounts recoverable for injury is a commonplace.

The question was before this Court in the *Workmen's Compensation* cases. In *New York Central R. R. Co.* v. *White,* 243 U. S. 188, the New York act was considered. Because a new and workable, though rigid, amount of recovery was substituted for the indeterminate damages hypothetically recoverable in a negligence action, it was urged upon this Court

> "That the employee's rights are interfered with, in that he is prevented from having compensation for injuries arising from the employer's fault commensurate with the damages actually sustained, and is limited to the measure of compensation prescribed by the Act" (at p. 196).

In rejecting the argument, this Court concluded that there was no valid objection to a statutory limitation of amounts recoverable on the ground that sums in excess of those amounts *might* be recovered at common law:

> "* * * Nor can it be deemed arbitrary and unreasonable, from the standpoint of the employee's interest, to supplant a system under which he assumed the entire risk of injury in ordinary cases, and in others had a right to recover an amount more or less speculative upon proving facts of negligence that often were difficult to prove, and substitute a system under which in all ordinary cases of accidental injury he is sure of a definite and easily ascertained compensation, not being obliged to assume the entire loss in any case but in all cases assuming any loss beyond the prescribed scale" (at p. 204).

In that case the setting of legislative maxima of recovery was directly questioned. Yet there have been other

familiar examples, where the legislative power of limitation passed unchallenged. The various statutes derived from Lord Campbell's Act allow recovery for death by wrongful act. In some of these the recovery has been limited to $5,000. In others it is cut off at $10,000. So far from being questioned on constitutional grounds, the standard set in these acts has been referred to by Federal courts as an aid to fixing the damages for death in jurisdictions having no limitation. *Cheatham* v. *Red River Line,* 56 Fed. 248; *The Oceanic,* 61 Fed. 338; *Farmers' Loan & Trust Co.* v. *Toledo etc. Ry. Co.,* 67 Fed. 73.

Again, the original Federal statute limiting liability of ship owners provided that liability should not exceed the interest of the owner in the ship and her freight (L. 1851, ch. 43; 9 Stat. 635; see 46 U. S. C. 183). This limitation was repeatedly enforced by this Court. *Norwich Company* v. *Wright,* 13 Wall. 104; *Providence & New York Steamship Co.* v. *Hill Mfg. Co.,* 109 U. S. 578; *Butler* v. *Boston Steamship Co.,* 130 U. S. 527.

Petitioners' brief (at p. 46) cites an instance in which the courts have held invalid an *unreasonable* restriction upon amounts recoverable. The Pennsylvania statute in question limited the amount to be recovered in certain personal injury suits to $3,000. In *Kay* v. *Pa. R. R. Co.,* 65 Pa. St. 269, this provision was declared inoperative, since retrospective, where suit was brought before its passage. In the second case, *Passenger Railway Co.* v. *Boudrou,* 92 Pa. St. 475, a jury had rendered a verdict for $10,000 against the railroad. The lower court's disregard of the limitation was upheld, two judges dissenting. On the ground that the plaintiff's remedy at common law for personal injury could not be thus summarily curtailed, the prevailing opinion said:

> "The people have withheld power from the legislature and the courts to deprive them of that remedy, or to circumscribe it so that a jury can only give a pitiful fraction of the damage sustained" (at p. 482).

Cf. New York Central R. R. Co. v. *White, supra,* 243 U. S. 188.

Monongahela Navigation Co, v. *United States,* 148 U. S. 312, also stands for an entirely different principle, in that there an entire item of loss (loss of franchise value) had been arbitrarily rejected by Congress in providing for recovery under exercise of the powers of eminent domain.

The case of *East Kingston* v. *Towle,* 48 N. H. 57, also cited at page 45 of the petitioners' brief, decided only that a defendant could not be made liable for damages assessed in an *ex parte* non-judicial proceeding to which he was not a party.

Petitioners' cases throw into relief the validity of a reasonably conceived substitute for a plaintiff's former remedy, especially where the former remedy was admittedly inadequate as a practical matter, as was the plight of landlords with bankrupt corporate tenants.

Congress has provided a fair equivalent so that there may be a final determination of an otherwise contingent and speculative claim.

(C)

Application of these Principles and Authorities to the Facts of this Case.

Under the terms of the claimants' lease neither the amount, nor indeed the existence, of their loss will become

certain until late in the term,—perhaps even at its end (March 31, 1946). *Hermitage* v. *Levine,* 248 N. Y. 333. The covenant here was not to pay liquidated damages in the event of bankruptcy (*cf. Wm. Filene's Sons Co.* v. *Weed,* 245 U. S. 597, and *Irving Trust Co.* v. *Perry Co.,* 293 U. S. 307), but only to indemnify the claimants for any loss suffered during the term (R. 58). The Circuit Court of Appeals has stated, in *In re Outfitters' Operating Realty Co.,* 69 Fed. [2d] 90, 91, that such a covenant "requires the lessor to wait until the end of the term", the covenant *not* being, as this Court has expressly held (*Manhattan Properties, Inc.* v. *Irving Trust Co., supra,* at p. 338):

> "the equivalent of an agreement that bankruptcy shall be a breach of the lease and the consequent damages to the lessor be measured by the difference between the present value of the remainder of the term and the total rent to fall due in the future."[11]

The claimants make light of the difficulty of presently evaluating the loss which may accrue to them in 1946 and

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[11]In an endeavor to raise the constitutional issue more acutely, the petitioners have framed their proof of claim as if their lease contained such a damage clause (R. 6-7). In *Miller* v. *Irving Trust Co.,* 296 U. S. 256, this Court had the following to say of another landlord who tried to improve his position in the same fashion:

> "The petitioner's statement of claim does not follow the covenant in his lease. It is made as if it rested on a covenant providing for damages equal to rents reserved less rental value for the rest of the terms, such as that on which the landlord prevailed in *Irving Trust Co.* v. *Perry Co.,* 293 U. S. 307. But petitioner's claim must be adjudged on the basis of the covenant that in his interest was inserted in the lease * * *."

completely ignore the possibility that in the end there may be no net loss at all. But it is this latter element of contingency which is the more serious. As Judge Learned Hand said for the Circuit Court of Appeals, in *In re Outfitters' Operating Realty Co., supra,* 69 F. [2d] at page 91:

> "It is the uncertainty in fact of the loss that invalidates the claim * * *."

CONCLUSION

It is respectfully submitted that the judgment of the Circuit Court of Appeals should be affirmed.

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DEC 12 19
CHARLES ELMORE

Supreme Court of the United States

October Term, 1936.

No. 354

IN THE MATTER

OF

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as Trustees,
Petitioners,

against

GRAYSON M.-P. MURPHY, et al., as a Preferred Stockholders Protective Committee, et al.,
Respondents.

On Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

BRIEF FOR RESPONDENT PREFERRED STOCKHOLDERS PROTECTIVE COMMITTEE

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BRIEF FOR RESPONDENT PREFERRED STOCKHOLDERS PROTECTIVE COMMITTEE.

Opinions Below.

The opinion of the District Court appears at page 146 of the record and is not officially reported. The opinion of the Circuit Court of Appeals is reported at 85 F. (2d) 35.

Statement of Case.

In 1926 Petitioners' predecessors in title leased premises located at Trenton, New Jersey, to the Debtor for a term of twenty years under a lease containing the following provision:

> "* * * these presents are upon this covenant, that if the Tenant * * * shall be adjudicated bankrupt or insolvent according to law, or if any assignment of its property shall be made for the benefit of creditors, then and in any of said cases the Landlord lawfully may enter into and upon the said premises * * * without being deemed guilty of any manner of trespass, and without prejudice to any remedies which might otherwise be used for arrears of rent or preceding breach of covenant, and upon entry as aforesaid this lease shall determine and the Tenant covenants that in case of such termination it will indemnify the Landlords against all loss of rent which the Landlords may incur by reason of such termination, during the residue of the term above specified" (R. 57-58).

The Debtor was adjudicated a bankrupt on August 29, 1932. The Debtor's Trustee in Bankruptcy disaffirmed the lease on November 14, 1932. Thereupon, Petitioners reentered the premises (R. 40-41). This re-entry terminated the lease (Petitioners' Brief, p. 6).

On June 14, 1934, the filing by the Debtor of its petition for reorganization under Section 77-B of the Bankruptcy Act was approved (R. 40). The Petitioners filed a claim in these proceedings for $90,212.91, being the alleged rent payable under the lease, including estimated taxes, for the residue of the term specified, less the alleged rental value (as of August 29, 1932) for the same period (R. 6-7, 73-74).

The Debtor's Trustee objected to the claim as filed and asked that it be limited to an amount limited by the statute. Upon the hearing the Trustee conceded that the Petitioners' damages would equal the statutory maximum (R. 19).

The Preferred Stockholders Committee and the Debentureholders Committee (intervenors in the proceedings) objected

to the allowance of the claim in any amount over the rental due at the termination of the lease for the reason that it was uncertain whether the Landlords would suffer any loss (R. 20-21). The evidence presented on behalf of the Petitioners as to the re-rental value of the premises was objected to as irrelevant and immaterial (R. 21), and evidence was presented to show that there was no reason to believe that the rental value of the premises was permanently impaired. Specifically, this evidence showed that the premises covered by the lease are located in the business center of Trenton, New Jersey, and are desirable for any retail business, and that so far as can be determined the location will continue to be one of the best locations in that city (R. 29-37).

The Special Master recommended that the claim should be allowed as a general claim in the amount of $44,377.55 (being an amount equal to three years' rent, including taxes, from the date of the Landlords' re-entry upon the premises, plus the rent and taxes which had accrued to the time of such re-entry), but that all questions as to the excess of their claim should be reserved until the time of the classification of creditors and stockholders according to the nature of their respective claims and interests, and the consideration of a plan of reorganization (R. 93).

The District Court (Knox, J.) confirmed the allowance of the claim in the amount of the statutory maximum, but held that such maximum was the extent of the Petitioners' right to participate in these proceedings (R. 116-118). The Court of Appeals affirmed the order of the District Court.

Petitioners appeal from so much of the order as limits their claim to $44,377.55 and argue that the provision of Section 77-B of the Bankruptcy Act, which limits the amount for which future rent claims may be proved, is unconstitutional.

Statute Involved.

Section 77-B (b) (10) provides in part as follows:

> "The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of re-entry of the landlord, whichever first occurs, whether before or after the filing of the petition; plus unpaid rent accrued up to such date of surrender or re-entry * * *."

Summary of Argument.

This brief will be devoted to consideration of the constitutionality of the statute. The memorandum opinion of the District Court admirably summarizes the argument in support of the statute.* Judge Knox said:

> "In my opinion, the provisions made by Section 77 b for the allowance of claims of landlords upon breached real estate leases were intended to put at rest the interminable speculative considerations that had to be taken into account in arriving at damages growing out of broken leases. In a proposed reorganization it is essential that claims be known and fixed at an early date—it is better that damages be fixed arbitrarily, as was done, than they should depend upon the attempts of parties in interest, assisted by experts, to read the future" (R. 146).

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* No appeal has been taken to this Court from the allowance of the claim for the amount equal to the three year maximum, although in the courts below we urged that the Petitioners are not holders of a claim which may be presently liquidated.

I.

The limitation imposed by Section 77-B of the Bankruptcy Act upon contingent rent claims is reasonable and constitutional.

The Petitioners would seem to be "creditors" under the broad definition of that term contained in Section 77-B (b) (10) and the provision of the statute quoted above evidences an intention that some valuation should be placed upon the contract right of the Petitioners for the purposes of a plan of reorganization terminating the Debtor's liability under such contract. The compensation to be allowed for the termination of the Petitioners' right must depend, however, upon the nature of their contract.

The default clause of the lease between Petitioners and the Debtor, quoted above at page 2, is similar to that construed by this Court in *Brown* v. *Irving Trust Co.* (*Manhattan Properties* case), 291 U. S. 320, 338. On similar facts the Court there concluded that the bankruptcy of the lessee did not of itself terminate the lease, that the lease was terminated by the landlord's re-entry, that this re-entry brought to life the contract of indemnity, that the bankruptcy of the lessee did not breach the contract of indemnity and that by its terms no liability would arise on the contract of indemnity until the expiration of the original term. These views are reaffirmed in *Miller* v. *Irving Trust Co.*, 296 U. S. 256, where the Court took the position with regard to a claim based on a similar covenant that, until the expiration of the original term, it would be a mere matter of speculation whether any liability ever would arise.*

Not only may rental values be so enhanced that the landlord will suffer no ultimate loss, but the right to indemnity may be altogether lost or forfeited by any one of a number of contingencies, none of which is by any means remote, to wit, occupation of the premises by the landlords for their own purposes (*Cannon* v. *56th Street Garage, Inc.*, C. C. A. 2d, 45 F. [2d] 110), voluntary transfer of the premises by

* The *Miller* case dealt with a lease of New Jersey premises.

the landlords (*Seidlitz* v. *Auerbach*, 230 N. Y. 167, 175), condemnation of the landlords' property by public authorities, or loss by the landlords of their property through mortgage foreclosure or sale for taxes.

If it is a mere matter of speculation whether any liability will ever arise under the agreement which is to be terminated by the reorganization decree, it is reasonable that Congress should place a limitation upon any compensation to be paid for the termination of the possible liability. The degree of the contingency of the liability obviously depends upon the length of the term of the contract and upon many other factors. It was not desirable, therefore, that Congress should attempt to lay down fixed rules for the determination of the compensation to be awarded, but rather that some limitation should be placed upon the damages which might be assessed and that rights against the Debtor should be speedily adjusted with a minimum of litigation.

The Petitioners, by the covenant inserted in the lease in their interest, expressly excluded the right to *damages* for the breach of the lease and elected to rely on indemnity against loss even in the case of the bankruptcy or insolvency of the lessee corporation. The Petitioners' right depends on the adequacy of the covenant (*Gardiner* v. *Butler*, 245 U. S. 603, 605). Damages in the measure sought by the Petitioners bear no relation to the liability assumed by the lessee. The covenant is to indemnify against loss of rent, and, at common law, future rents are not susceptible of commutation and conversion into present debts (*Jersey Blvd. Corp.* v. *Lerner Stores Corp.* [Ct. of App. of Md., 1936, not yet officially reported], 178 Atl. 707). Granting that the right of claimants under such a covenant should be recognized in a reorganization, it was fair to place a limitation upon the speculative damages which might be assessed, growing out of the "attempts of parties in interest, assisted by experts, to read the future." It was not the intention of Congress that the Debtor should be penalized by the imposition of liabilities not assumed by it. Nor is it desirable or practicable to reserve rights based upon such contingent contracts. In many cases, new money must be raised for the

purposes of the reorganization by the assessment of stockholders, and the parties advancing money to the reorganized company should be apprised of the extent of that corporation's liabilities.

Petitioners must strain to present a picture of a capricious and harsh statute. The very changes made by the Senate and House Committees in the provision under attack indicate deliberation upon the fair compensation to be awarded to claimants such as the Petitioners. To allow, as in this case of a net lease, damages equal to the unpaid rent and taxes to date of re-entry plus rent and taxes payable for a period of three years thereafter is indeed to allow damages in a measure which parties making a new lease might regard as unduly harsh to the tenant.

"Section 77-B is based on equitable recognition of the rights of all who have an interest in a common property * * *." "Like other constitutional grants of power, that giving Congress power over bankruptcies is to be interpreted, not in the light of the conditions with which the framers of the Constitution were familiar, but of what is required under modern conditions to deal adequately with the relationship existing between embarrassed debtors and their creditors." "The statute is of a remedial character, designed to facilitate the reorganization of corporate business made necessary by the economic depression through which the country has been passing." "It is * * * no ground of constitutional objection that the Act relates only to corporate debtors." * "Every member of a political community must necessarily part with some of the rights which, as an individual not affected by his relation to others, he might have retained." (*Cont. Ill. National Bank & Trust Co. v. C., R. I. & P. Railway Co.*, 294 U. S. 648, 674.) If, under the bankruptcy clause, Congress may deal with debtors' rights as well as creditors' rights, the statute should be sustained. All contracts are made subject to such bankruptcy power.

Whether the statutory limitation is applicable in a case where the parties to the lease have stipulated liquidated damages for breach of a lease which may exceed three years'

* The language quoted above is from the opinion of the Circuit Court of Appeals for the Fourth Circuit in *Campbell* v. *Alleghany Corp.*, 75 F. (2d) 947, cert. den. 296 U. S. 581.

rent, we do not undertake to say. No cases are shown to be now pending involving such question. As Judge Hand points out, to challenge a statute one must suffer a personal grievance (R. 154). We suggest, however, that Congress has the *power* under the bankruptcy clause to disregard a measure of damages fixed by the parties if that measure would work an unequal distribution, even though the provision would not otherwise be regarded as one stipulating a penalty. The exercise of such power might result in impairing contracts to different extents, but in nearer equality of compensation.*

There can be no division of the claim by allowing a part and reserving a part. The claim is indivisible (*Hermitage* v. *Levine*, 248 N. Y. 333, 338). Neither may any portion of the claim be reserved for consideration in connection with a plan of reorganization, a suggestion made by some landlords in order to obtain a trading advantage in connection with negotiating a plan. The District Court answered this suggestion, saying that in "a proposed reorganization it is essential that claims be known and fixed at an early date."

CONCLUSION.

We submit that the order appealed from should be affirmed.

Respectfully submitted,

SANFORD H. E. FREUND,
WINTHROP H. KELLOGG,
DOUGLAS B. STEIMLE,
Counsel.

SHEARMAN & STERLING
AND
BERLE & BERLE,
Attorneys for Preferred Stockholders Protective Committee.

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* That the instant case is the only one so far reported in which the constitutionality of the limitation has been contested, despite the great number of reorganizations involving leases, indicates that the statute provides a practical means of adjusting landlords' claims.

Office - Supreme
FILE
DEC 8
CHARLES ELMOR

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 354.

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as trustees,
Petitioners,

GRAYSON M.-P. MURPHY, *et al.*, as a Preferred Stockholders Protective Committee, *et al.*,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR INTERVENOR JACOB RUPPERT REALTY CORPORATION.

M. CARL LEVINE,
Counsel for the Intervenor.

M. CARL LEVINE,
DAVID MORGULAS,
Of Counsel.

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Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF OF JACOB RUPPERT REALTY CORPORATION AS AMICUS CURIAE.

The Jacob Ruppert Realty Corporation is a landlord-creditor in these proceedings, having been granted the right to intervene on behalf of a large group of landlord-

claimants, at or about the time the debtor's petition was filed. This brief is filed with the consent of all parties to this proceeding.

The Jacob Ruppert Realty Corporation claim was allowed to the limited extent of three years' damage, in the amount of $219,983.30, without prejudice to whatever right the Jacob Ruppert Realty Corporation had, prior to confirmation of a plan of reorganization, to prove further damage in priority to the interests of stockholders. The order allowing the Ruppert claim is set forth in the appendix.

The Ruppert claim will not be further referred to, all references being to the petitioners' claim.

THE QUESTION.

If the petitioners or any other landlords can prove that they have been damaged in excess of the three-year maximum allowable on a parity with claims provable under Section 63A of the Bankruptcy Act,* should that excess damage claim have a prior right to the remaining assets of the debtor's estate before stockholders can receive any consideration?

THE STATUTE.

Section 77B of the Bankruptcy Act provides:

> "Sec. 77B. Corporate Reorganizations * * *.
>
> (b) * * * (10) The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory con-

* The term "three year maximum", as used herein, includes accrued unpaid rent up to the date of surrender or re-entry as provided in the statutory formula.

tracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts * * * or other interest of whatever character. * * *

In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section, any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of re-entry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or re-entry. * * * "

(Act approved June 7, 1934, 48 St. 911, Ch. 424, Sec. 1; U. S. C. Tit. 11, Sec. 207.)

THE OPINIONS BELOW.

The Special Master recommended that the petitioners' claim for damages for breach of the indemnity covenant in the lease be allowed on a parity with debts provable under Section 63A of the Bankruptcy Act to the extent of three years' rent, and that all questions as to the balance of the claim should be reserved until the time for the classification of creditors and the consideration of a plan of reorganization (R. 88, 93).

The District Court modified the Special Master's report in that it completely limited the claim to the extent of the three years' rent provable on a parity with debts under Section 63A of the Bankruptcy Act and barred consideration of the balance of the claim (R. 116-118).

The Circuit Court of Appeals affirmed the order of the District Court (R. 150), 85 F. (2d) 35.

SUMMARY OF ARGUMENT.

POINT I

A landlord is entitled to prove as against stockholders any and all damages sustained in excess of the three year maximum allowed on a parity with other debts provable under Section 63A of the Bankruptcy Act.

POINT II

In any event, the Special Master correctly ruled that the petitioners' claim for damages sustained in excess of the three year allowance on a parity with debts provable under Section 63A of the Bankruptcy Act should be reserved until creditors were classified and a plan of reorganization considered.

ARGUMENT.

POINT I

A landlord is entitled to prove as against stockholders any and all damages sustained in excess of the three year maximum allowed on a parity with other debts provable under Section 63A of the Bankruptcy Act.

The rights of neither bondholders nor general creditors are involved.

The issue narrows itself to whether stockholders shall acquire whatever balance of assets remains after payment to bondholders and creditors on a parity with them, while landlords must forfeit their right to indemnity for any damages sustained in excess of the three-year allowance.

Section 77B contains only one provision affecting the rights of landlord-claimants (sub. b [10]):

> "The Claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under Sec. 63 (a) of this act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry."

The Act does not limit the complete provability of a landlord's claim as against stockholders.

It is important that the Act directs that the claim be "treated" on a parity with debts provable under Section

63A to the extent of three years' rental. By using the word "treat" in relation to such debts it is obvious that a landlord's claim was being divided into two categories: (a) in relation to debts provable under Section 63A there was to be a limitation; (b) in relation to all other debts and rights there was to be no limitation. Any other interpretation would give no consideration whatsoever to the use of the word "treated".

It is indeed highly significant that at the same time Section 77B was enacted, Section 63A of the Bankruptcy Act was also amended by adding subdivision (7) thereto so as to make a landlord's claim for damages provable in bankruptcy to the extent of one year's rent, viz:

> "and (7) claims for damages respecting executory contracts including future rents whether the bankrupt be an individual or a corporation, but the claim of a landlord for injury resulting from the rejection by the trustee of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall in no event be allowed in an amount exceeding the rent reserved by the lease, without acceleration, for the year next succeeding the date of the surrender of the premises plus an amount equal to the unpaid rent accrued up to said date."

It is apparent that when Congress intended a direct limitation it was so stated in unmistakable language by the use of the following:

> "Shall in no event be allowed in an amount exceeding * * *."

If Congress intended that a landlord's claim should be limited in 77B proceedings to three years' rent, it would have so specifically provided, just as a direct limitation was provided by the aforesaid amendment to Section 63A. The use of the word "treated" in the 77B amendment as against the language of direct limitation in 63A renders

impossible any interpretation which would require a limitation of a landlord's claim as against stockholders.

The factual situation in this very proceeding makes the stockholders' contention incredible. At the time that the debtor filed its petition for reorganization (June 14, 1934), the debtor was in bankruptcy and 50 percent in dividends had already been paid. There were more than enough remaining assets to fully pay all provable and allowed bankruptcy claims and leave the business intact for contingent creditors, of whom the landlords were undoubtedly the largest class. Although landlords had no provable claims in bankruptcy, yet their claims survived bankruptcy and were still fully intact and existent in the event there was a surplus after payment of all claims provable in bankruptcy. That surplus belonged to the landlords to the complete exclusion of the stockholders. Under these circumstances contingent creditors would have been enabled to fully prove their entire damage claims before stockholders could receive anything.

Northern Pacific Ry. Co. v. *Boyd*, 228 U. S. 482.

By the enactment of 77B, Congress certainly did not intend to diminish the rights of landlords. If anything, the statute sought to benefit landlords and make their claims provable even on a parity with bondholders, but limited to a maximum of three years' rent. Nothing was said, however, about the balance of a landlord's claim for it was hardly conceivable that a company which could pay general creditors and bondholders 100 percent, landlord-creditors 100 percent of their three-year maximum and could still have sufficient assets remaining would avail itself of Section 77B. Yet, that is the situation at bar. It can hardly be urged that under such circumstances landlords are to forego recoupment of their total loss by making a gift to stockholders.

Legislative acts must be construed so as to prevent any unconstitutional results. *United States* v. *Delaware & Hudson,* 213 U. S. 366. To argue that Congress intended to deprive one class of creditors of their property rights and make an outright gift to stockholders is tantamount to saying that Congress enacted class legislation and deprived landlords of their property without due process. No such interpretation can be indulged in unless there is explicit language to that effect. The most that can be said for the stockholders' position is that the statute might be susceptible of two interpretations. If that be so, the one which would render the statute clearly constitutional must be adopted as against an interpretation which would render its constitutionality doubtful.

Arkansas National Gas Co. v. *Arkansas Railroad Commissioners,* 261 U. S. 379.

Section 77B was enacted to permit corporations to rearrange their debt and refund their obligations but not to permit them to wipe out their debt or scale it down when there were sufficient assets to meet claims in full.

Any other construction of the Act would place landlords at the mercy of any large company which under a threat of reorganization could compel landlords to accept three years' rent as the full value of any long term lease, even though the corporation was fully able to meet all claims in full.

Unquestionably, landlords were entitled to collect their full damages in priority to stockholders, prior to the enactment of 77B, if there were sufficient assets left after provable claims were paid. No construction should be adopted which would deprive landlords of rights they already had, and transfer the benefits of those rights to stockholders.

POINT II

In any event, the Special Master correctly ruled that the petitioners' claim for damages sustained in excess of the three year allowance on a parity with debts provable under Section 63A of the Bankruptcy Act should be reserved until creditors were classified and a plan of reorganization considered.

The Special Master disposed of the contention at bar as follows (R. 88):

> "Whether the Landlords are entitled to an allowance in excess of the three years' period, in subordination to the provable claims, but in priority to stockholders, is not required to be determined at this time. Whether there will be a surplus over and above the amount of provable claims and expenses of administration, how the same is to be distributed and, in fact, the method of payment and manner thereof to the various creditors, will depend upon the classification of creditors, and the respective rights of the various interested parties herein. All these matters will only be presented when the time for classification arrives, and when various questions arise in the consideration and the confirmation of any plan of reorganization. Accordingly I will adopt the suggestion of the Trustee and the opposing Intervenors, and will leave the question as to the allowance of any excess claim for future consideration, as aforesaid."

The claim of the petitioners for damages over the three-year allowance could only have meaning if a surplus of assets remained after payment of the allowable claims. Before it is evident that a surplus exists, discussion about priorities between landlords and stockholders is academic. The Special Master must have felt that it was premature to argue about dividing assets until the record indicated

there was something to argue about and he accordingly decided that the question could not be determined until creditors were classified and a plan of reorganization considered. Then all the equities of the different parties and different groups could be considered, and the remedial purposes of Section 77B readily applied.

It was our contention, in the Courts below, that it would have been most expedient to reserve the consideration of the question at bar to a time when full inquiry could be made as to the fullest extent of the debtor's assets. So important a problem as the one at bar cannot be correctly dealt with until the complete picture of the debtor's situation has been presented to the Court.

The Preferred Stockholders' Committee has consistently argued that the principles enunciated by this Court in *Northern Pacific Ry.* v. *Boyd* (supra) do not conflict with limitation of the landlords' claims urging that the three-year limitation is in effect the embodiment of a fair plan. What is fair in one case, however, would be wholly unfair in the other. If there are sufficient assets left after payment of creditors, bondholders and landlords limited to three years' rent, to make the preferred stock have a fair book value of $50 per share or more, it is unreasonable that the preferred stockholder should thus profit before the landlord's loss has been made whole. Especially so, when the great bulk of present stockholders have undoubtedly purchased their holdings at a fraction of par. It must be remembered that landlords seek recoupment of their losses, while the average stockholder seeks a profit out of his speculation or investment.

This Court has repeatedly held that it would not pass on the constitutionality of statutes unless the party claimed to be aggrieved has shown that he has been deprived of a constitutional right, whether of person or of property. In the present case the question as to whether or not the

landlord's excess claim is to be considered in priority to stockholders can have no importance until the record affirmatively shows that there is a surplus in the estate after the payment of all prior debts. The fact that the petitioner may have a claim does not mean that the claim is worth one cent until the record indicates what the assets of the estate are as against its provable claims.

We respectfully urge that in light of the present record, the question as to allowance of any additional damage to landlords over their three-year allowance should have been reserved until a consideration of a plan of reorganization, as suggested by the Special Master. In that manner, all questions as to constitutionality are avoided.

The Circuit Court of Appeals completely overlooked this principle. Without a record disclosing the complete story of the debtor's financial position, it entertained and decided constitutional questions which undoubtedly deprived many landlord-claimants in this proceeding of their right of indemnity without any opportunity to present the facts and show the unfairness of a ruling which but deprives one class of creditors of their right of recoupment for the benefit of the owners of the corporation.

It is respectfully submitted that the judgment of the Circuit Court of Appeals should be reversed insofar as it limited petitioners' claim to a three year limitation, and that petitioners' claim to any damages in excess of the three year maximum already allowed on a parity with debts provable under Section 63A of the Bankruptcy Act be either allowed in priority to rights of stockholders or be reserved for consideration in a plan of reorganization, as suggested by the Special Master.

Respectfully submitted,

M. Carl Levine,
Counsel for the Intervenor,
Jacob Ruppert Realty Corporation.

M. Carl Levine,
David Morgulas,
Of Counsel.

December 2, 1936.

APPENDIX A

DISTRICT COURT OF THE UNITED STATES,

SOUTHERN DISTRICT OF NEW YORK.

IN THE MATTER OF UNITED CIGAR STORES COMPANY OF AMERICA, Debtor.	In Proceedings for Reorganization of a Corporation. No. 59,886.

Upon reading and filing the petition of Irving Trust Company, trustee of the estate of the above-named debtor, verified May 24, 1935, the notice of motion thereon dated May 24, 1935, and the affidavit of Lewin L. Vinton verified May 24, 1935, as to the mailing of said petition and notice of motion to the attorney for the claimant referred to in said petition, and to the attorneys for the intervenors in these proceedings, and the matter having duly come on to be heard before this Court on the 9th day of July, 1935, in pursuance of said notice of motion, and there being no opposition to the granting of said petition,

It is, on motion of Cravath, DeGersdorff, Swaine & Wood, attorneys for said trustee,

REPORTED AND RECOMMENDED that the claim set forth in the proof of claim numbered 5017 and filed herein by Jacob Ruppert Realty Corp. be reduced to and finally allowed in these proceedings in the principal amount of $219,983.30, provided, however,

(1) that such allowance shall be without prejudice in any respect whatever to the right, if any, of said

claimant to secure the allowance of its claim numbered 5017, prior to the confirmation of a plan of reorganization herein, in a further sum representing the difference between (a) the amount of said claim allowable under Section 77B of the Bankruptcy Act, as amended, on a parity with debts which would be provable under Section 63 (a) of said Act and (b) the total amount of claimant's damages for the entire term of the lease upon which said claim is based, in subordination to debts provable under said Section 63 (a) but in priority to the interests of holders of preferred stock and common stock of the debtor herein, and without prejudice to any right of the trustee or any intervenor in these proceedings to oppose the allowance of said claim in any such further sum;

(2) that if it shall be finally determined in any proceeding herein in which the claimant attempts to prove damages with respect to its claim numbered 5017 in a further sum than said amount of $219,983.30, that the total amount of damages for the entire term of the lease upon which said claim is based is less than the sum of $219,983.30, then the amount for which the claim is hereby allowed shall be further reduced to the amount of damages for the entire term of the lease; and

(3) that the determination whether the claimant has the right reserved for future determination as provided in (1) above shall be governed by the final decision of this Court or (if appealed from) any higher Federal Court in the matter of any other claim in this proceeding involving such question.

Dated, New York, N. Y., July 18, 1935.

IRWIN KURTZ,
Special Master.

APPENDIX B

SUPREME COURT OF THE UNITED STATES

In the Matter of

UNITED CIGAR STORES COMPANY OF AMERICA,

Debtor,

CAROLINE R. KUEHNER and FREDERICK G. FISCHER, as Trustees,

Petitioners in No. 354.

IT IS HEREBY STIPULATED AND AGREED that the JACOB RUPPERT REALTY CORPORATION, one of the intervenors in the above entitled proceeding, be permitted to file briefs amicus curiae in the above entitled appeal.

Dated, New York, November 9th, 1936.

M. CARL LEVINE,
Attorney for Jacob Ruppert
Realty Corporation.

ROLLIN BROWNE,
RALPH MONTGOMERY ARKUSH,
HENRY L. GLENN,
Counsel for petitioners Caroline R.
Kuehner and Frederick G. Fischer,
in cause No. 354.

MITCHELL, TAYLOR, CAPRON & MARSH
and
RALPH MONTGOMERY ARKUSH,
Counsel for respondent Landlords' Protective Committee.

SHEARMAN & STERLING
and
BERLE & BERLE,
Counsel for respondent Preferred Stockholders' Protective Committee.

DAVIS, POLK, WARDWELL, GARDINER & REED,
Counsel for respondent Debenture-holders' Protective Committee.

MILBANK, TWEED, HOPE & WEBB,
Counsel for respondent Phoenix Securities Corporation.

WRIGHT, GORDON, ZACHRY & PARLIN,
Counsel for respondent Reorganization Committee.

CRAVATH, DE GERSDORFF, SWAINE & WOOD,
Counsel for Trustee.

SUPREME COURT OF THE UNITED STATES.

No. 354.—October Term, 1936.

Caroline R. Kuehner, et al., Trustees, Petitioners, *vs.* Irving Trust Company, Trustee of the United Cigar Stores Company of America, et al.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[January 4, 1937.]

Mr. Justice Roberts delivered the opinion of the Court.

In this case we are concerned with that portion of subsection (b) (10) of Section 77B of the Bankruptcy Act which limits the claim of a landlord for indemnity under a covenant in a lease to an amount not to exceed three years' rent.

The questions are: (1) Is the claim so limited in all events and for all purposes or is the surplus over the specified amount, though subordinated to the claims of other creditors, to have priority over the interests of stockholders or to be reserved as a liability of the reorganized corporation? (2) If the claim is limited in all events to the named amount, is the provision obnoxious to the Fifth Amendment of the Constitution?

The petitioners leased real estate to United Cigar Stores Company in 1926 for a term expiring in 1946. August 29, 1932, the company was adjudicated a voluntary bankrupt. November 14, 1932, the trustee rejected the lease and abandoned the premises. The following day the petitioners reentered and terminated the leasehold in accordance with the provisions of the lease which contained a covenant by the lessee to indemnify them against all loss of rent from such termination. Immediately upon adoption of Section 77B the bankrupt filed its petition for reorganization thereunder, which was approved by the court.

The petitioners presented a proof of claim, measuring the injury resulting from the termination of the leasehold by the difference

between the rental value and the value of the rent reserved for the remainder of the term. They prayed that the amount claimed be ranked on a parity with other provable debts to the extent of three years' rent and, as to the balance, be subordinated to other provable debts but awarded priority over the claims or interests of the debtor's stockholders. The trustee asked that the allowance be in an amount limited as provided by the statute. Committees representing preferred stockholders and debenture holders objected to allowance of the claim in any amount, asserting the petitioners could not sue on the covenant of indemnity under the state law until the expiration of the term and, having no presently enforceable claim under state law, had none in the reorganization proceeding. The petitioners amended their pleading by adding a prayer that to the extent any portion of the claim might be held not allowable a charge be reserved against the debtor's assets for such portion in priority to any interest accorded stockholders.

The uncontroverted testimony is that the fair rental value for the balance of the term is $111,545.36. The future instalments of rent to the end of the term aggregate $199,237.66. A special master recommended that the petitioners' claim be allowed and liquidated at the amount of the difference between present rental value and present value of the rent reserved. He found that the sum so ascertained would be not less than the equivalent of three years' rent and recommended allowance of the claim on a parity with provable debts to the extent of three years' rent,—$44,377.55,—and the reservation of all questions as to the balance until the time for classification of creditors and consideration of a reorganization plan. The District Court confirmed the master's report save that it decided the claim as allowed should represent the extent of claimants' right to participate in the proceedings. Cross appeals were taken to the Circuit Court of Appeals which held that petitioners had a provable claim, that the method adopted for the liquidation of the claim was proper, that Section 77B required limitation of allowance to a sum not in excess of the three years' rent mentioned in the statute and that such limitation does not take petitioners' property without due process of law in violation of the Fifth Amendment.[1] We granted certiorari because of the importance of the questions involved.

[1] 85 F. (2d) 35.

The respondent Stockholders' Committee does not now deny that the petitioners have a provable claim but joins the trustee in support of the decision below that the allowance must be limited for all purposes of the proceeding to three years' rent.

We have held in *City Bank Farmers Trust Company* v. *Irving Trust Company*[2] that the broad definition of creditors in Section 77B gives the petitioners a provable claim for breach of the debtor's covenant of indemnity. The section, however, limits the amount for which such a claim may be allowed. The relevant provision, so far as applicable to petitioners' claim is:

"The claim of a landlord . . . for . . . indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding . . . . the date of reentry of the landlord, . . ."

The legislative history of this provision, and the successive alterations of its wording in both houses of Congress and in conference, to which we are referred, cannot affect its interpretation, since the language of the act as adopted is clear. The only phrase to which petitioners point in support of their contention that the claim is to be divided into two parts, one for an amount not exceeding three years' rent, to stand on a parity with other provable claims, and the other, representing the balance, to be subordinated to creditors' claims, but preferred to the interest of stockholders, is: "shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a)." We need not consider the suggestion that the words "on a parity" were left in the clause *per incuriam* when formulation of an earlier draft was altered, since, in our opinion, their presence however they came to be inserted, cannot overcome the direct mandate that "the claim . . . shall be limited." We agree, therefore, with the Circuit Court of Appeals that if, upon liquidation by deduction of present rental value from the present value of rent reserved, the difference exceeds the amount of the total rent for the three years succeeding the landlord's reentry, the claim may be allowed only for that amount.

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[2] No. 260, decided this day.

A more serious question is raised by the petitioners' insistence that thus applied the act exceeds legislative powers granted and infringes personal guaranties given by the Constitution. They say that the prescribed method will in some instances limit the amount allowed to a figure less than the landlord's actual ultimate loss, and thus partially destroy his remedy for enforcement of his contract. The resulting violations of the Constitution, they assert, are the transgression of the boundaries of the bankruptcy power vested in Congress, and the taking of their property without due process.

Is the enactment in excess of the power to legislate on the subject of bankruptcies, conferred upon Congress by Art. I, § 8, of the Constitution? Congress evidently considered the limitation imposed on claims of this class necessary or advantageous to a successful reorganization and its judgment is conclusive upon us, if the enactment is within its power.

The petitioners concede Congress has power to exclude contingent claims from proof and allowance so long as the obligations they represent are not extinguished by the statute.[3] They refer, however, to the statement in *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, that Congress has never attempted to supply a bankrupt with capital to engage in business at the expense of his creditors, as persuasive that a statute cannot discharge a bankrupt's assets from liability for his debts but can only discharge the bankrupt from encumbrances on his future exertions.[4] This principle, they assert, the statute violates. The short answer is that the object of bankruptcy laws is the equitable distribution of the debtor's assets amongst his creditors;[5] and the validity of the challenged provision must be tested by its appropriateness to that end. Congress, in determining what such an equitable distribution demands, is free to establish standards of provability and measures of allowance regardless of the claimant's ability to maintain an action in a court or the measure of his recovery in such an action if maintainable. The contested provision is within the power of Congress. The exercise of the power is, nevertheless, subject to the commands of the Fifth Amendment.[6]

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[3] Compare *Manhattan Properties, Inc.* v. *Irving Trust Company*, 291 U. S. 320, 332.

[4] See *Hanover National Bank* v. *Moyses*, 186 U. S. 181, 188.

[5] *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224, 227.

[6] *Louisville Joint Stock Land Bank* v. *Radford, supra*, p. 589.

Does the Act offend the due process guaranty by destruction of rights conferred by the petitioners' contract? They affirm that it does, not merely by impairing those rights but by a direct taking *pro tanto* of all remedies for their enforcement and, to that extent, of the contract itself. Conceding they have no lien upon, or property right in, the debtor's assets, such as was the subject of decision in *Louisville Joint Stock Land Bank* v. *Radford, supra,* they maintain that the Fifth Amendment assures them some effective procedure for the enforcement of the obligation of their contract; that the debtor's assets are a trust fund for creditors which cannot be invaded for the benefit of stockholders. As pointed out in the case last cited there is, as respects the exertion of the bankruptcy power, a significant difference between a property interest and a contract since the Constitution does not forbid impairment of the obligation of the latter. The equitable distribution of the bankrupt's assets, or the equitable adjustment of creditors' claims in respect of those assets, by way of reorganization, may therefore be regulated by a bankruptcy law which impairs the obligation of the debtor's contracts. Indeed every bankruptcy act avowedly works such impairment. While, therefore, the Fifth Amendment forbids the destruction of a contract it does not prohibit bankruptcy legislation affecting the creditor's remedy for its enforcement against the debtor's assets, or the measure of the creditor's participation therein, if the statutory provisions are consonant with a fair, reasonable, and equitable distribution of those assets. The law under consideration recognizes the petitioners' claim and permits it to share in the consideration to be distributed in reorganization. The question is whether the remedy is circumscribed in so unreasonable and arbitrary a way as to deny due process.

Bankruptcy originated as a seizure of the debtor's assets for equitable distribution amongst creditors. It was akin to a taking in execution. The concept was subsequently broadened to embrace the discharge of the embarrassed debtor from antecedent debts and to make the process available at his instance as well as at that of his creditors. Claims not provable, since they did not participate in the avails of the bankrupt's assets, were not discharged but remained recoverable by action against the discharged bankrupt. The object of Section 77 B was to extend the system to

permit and facilitate the reorganization of certain types of insolvent or embarrassed business corporations. The theory of the legislation is that the extension will serve the interests of the public, the creditors, and the shareholders.

If the bankruptcy act was to be broadened to embrace reorganization of corporate debtors the wisdom of relieving them of continuing liability for rent or under contracts of indemnity was apparent. And if the landlords' claims were to be discharged in the reorganization they must be admitted to participation on an equitable basis with other claims in shaping the reorganization and in distribution of that which is to go to creditors pursuant to any plan adopted. The section therefore made such claims provable. Its legislative history attests the diverse views entertained in Congress as to the amount for which a claim should be allowed. Only after mature deliberation was the limit set at the amount fixed in the act. The reasonableness of the limitation is to be determined in the light of all circumstances Congress might properly consider.

In *City Bank Farmers Trust Company* v. *Irving Trust Company* (No. 260, decided this day.), the peculiar and unfortunate status of landlords' claims under the Bankruptcy Act of 1898 is described. The tenant's bankruptcy removed all his assets from the reach of the landlord and left, as the latter's only remedy, suits against an empty corporate shell or a destitute individual. In framing the reorganization statute Congress obviously attempted to award landlords an equitable share in the debtor's assets as, in justice, it was bound to do since the purpose was to discharge the debtor from liability to future suits based upon the lease. It is incorrect to say that Congress took away all remedy under the lease. On the contrary, it gave a new and more certain remedy for a limited amount, in lieu of an old remedy inefficient and uncertain in its result. This is certainly not the taking of the landlord's property without due process.

But we are told that if Congress determined to admit landlords' claims to a share in debtors' assets it was bound by the Fifth Amendment not to be arbitrary in the allotment of such share or to discriminate between landlords and other creditors and between individual landlords. We cannot pronounce the limit set upon petitioners' claim arbitrary or unreasonable. It is well known that leases of business properties, particularly retail business prop-

erties, commonly run for long terms. The longer the term the greater the uncertainty as to the loss entailed by abrogation of the lease. Testimony as to present rental value partakes largely of the character of prophesy and, although that value is the cardinal factor in the measure of damages for which petitioners contend, it is obvious that, since the landlord is not bound to relet the premises for the unexpired term of the lease, that factor may have little real bearing upon the realities of the case. And, in any event, the possibility of the landlord's using the premises for his own purposes, their sale, their condemnation for public use, or their loss by foreclosure, renders an estimate of present rental value highly uncertain. Add to this the fact that bankruptcies multiply in hard times, and that estimates of rental value are made upon the basis of what a new tenant will pay in an era of economic depression, and the estimate becomes even more unreliable. Whatever courts, in the absence of a statutory formula, might feel compelled to adopt as the measure of damage in such a case, we cannot hold that Congress could not reasonably find that an award of the full difference between rental value and rent reserved for the remainder of the term smacks too much of speculation and that a uniform limit upon landlords' claims will, in the long run, be fair to them, to other creditors, and to the debtor.

The petitioners insist that the amount to which the claim must be limited has no reasonable relation to the facts; that a sum equal to three times the annual rent can have no relation to the probable loss by the ending of the leasehold. But the rent reserved, broadly speaking, has some relationship to the value of the property and the value of a lease thereon. What the statute does, is to assure at least three full years' rent to a landlord whose possible loss may exceed that amount, evidently upon the theory that with such an allowance the landlord stands a reasonable chance of restoring himself to as good a position as if the lease had not been terminated.

The petitioners say that by limiting their claim they are put upon a different basis from other creditors. A sufficient ground for the distinction is that petitioners get back their property. In other words, they have lost merely a bargain for the use of real estate whereas merchandise creditors, lenders, and others, recover in specie none of the property or money which passed from them to the debtor.

Finally, it is said that the statute is whimsical and arbitrary in that the limit fixed upon landlords' claims necessarily represents a

varying proportion of the actual loss of individual landlords and that this is discrimination of the most obvious sort. If, however, the statute does not deal unfairly with the petitioners it does not lie in their mouths to object because someone else perchance will receive a larger proportion of his ultimate loss as the same is ascertained years hence than will the petitioners. Congress, not unreasonably, felt that it was necessary, in the interest of expedition of proof and allowance of landlords' claims, which had never theretofore been permitted to share in a bankrupt debtor's assets, to fix a reasonable limit upon such claims. Naturally the amount fixed cannot bear the same relation to the ultimate loss or damage in every case. But it does not follow that, for this reason, all effort at uniformity of treatment of a peculiar class of claims, difficult of liquidation, is doomed to condemnation. All the arguments which petitioners submit would equally apply to any general and uniform formula for the limitation of such claims which the Congress might adopt. We are unable to say that that which Congress did select so discriminates between individual claimants to the detriment of the petitioners as to render it unconstitutional as to them.

The judgment is affirmed.

Affirmed.

Mr. Justice BRANDEIS took no part in the consideration or decision of this case.

A true copy.

Test:

Clerk, Supreme Court, U. S.